105TH CONGRESS 2D SESSION

H. R. 4700

To amend the Internal Revenue Code of 1986 to restructure and replace the income tax system of the United States to meet national priorities, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

OCTOBER 5, 1998

Mr. English of Pennsylvania introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to restructure and replace the income tax system of the United States to meet national priorities, and for other purposes.

- 1 Be it enacted by the Senate and House of Representa-
- 2 tives of the United States of America in Congress assembled,
- 3 SECTION 1. SHORT TITLE; AMENDMENT OF 1986 CODE;
- 4 TABLE OF CONTENTS.
- 5 (a) SHORT TITLE.—This Act may be cited as the
- 6 "Simplified USA Tax Act of 1998".
- 7 (b) Amendment of 1986 Code.—Except as other-
- 8 wise expressly provided, whenever in this Act a reference
- 9 is made to the Code or to a section or provision of the

- 1 Code, the reference shall be considered to be made to the
- 2 Internal Revenue Code of 1986 or to a section or provision
- 3 thereof.
- 4 (c) Table of Contents.—
 - Sec. 1. Short title; amendment of 1986 Code; table of contents.

TITLE I—FINDINGS; NEED TO REPLACE THE INCOME TAX

Sec. 101. Replacing the income tax of the United States.

TITLE II—SIMPLIFIED USA TAX FOR INDIVIDUALS

- Sec. 201. Simplified USA Tax for individuals.
- Sec. 202. Reorganization of the Code.

TITLE III—SIMPLIFIED USA TAX FOR BUSINESSES

- Sec. 301. Repeal of present corporate income tax; new tax paid by corporations and other businesses.
- Sec. 302. Repeal of chapter 6.

TITLE IV—DEFERRED COMPENSATION PLANS

- Sec. 401. Provisions saved.
- Sec. 402. Clerical Amendments.
- Sec. 403. Clerical Amendments.

TITLE V—REPEAL OF ESTATE AND GIFT TAXES

- Sec. 501. Repeal of gratuitous transfer taxes.
- Sec. 502. Effective Date.

TITLE VI—TECHNICAL AND ADMINISTRATIVE CHANGES; EFFECTIVE DATES

- Sec. 601. USA Tax Code.
- Sec. 602. Revisions to the Code.
- Sec. 603. Application of subtitle F.
- Sec. 604. Clerical amendment.

5 TITLE I—FINDINGS; NEED TO

6 REPLACE THE INCOME TAX

- 7 SEC. 101. REPLACING THE INCOME TAX OF THE UNITED
- 8 STATES.
- 9 (a) FINDINGS.—The Congress finds that—

1	(1) the current Tax Code is irreparably flawed
2	and must be replaced;
3	(2) to enhance the liberty and protect the pri-
4	vacy of individuals, the Tax Code must be made sim-
5	pler and nonintrusive, and it must be applied
6	evenhandedly to all;
7	(3) to be fair and to provide for the prosperity
8	of current and future generation, the Tax Code must
9	give all individuals at all income levels an oppor-
10	tunity to save, invest and raise their standard of liv-
11	ing and that of their children; and
12	(4) future economic growth requires a tax sys-
13	tem that facilitates successful competition in the
14	global marketplace.
15	(b) Main Features of Simplified USA Tax Sys-
16	TEM.—
17	(1) Replacement of old tax system.—
18	Chapter 1 of subtitle A (related to income taxes) of
19	the Code is repealed and replaced for years begin-
20	ning after 1998.
21	(2) Estate and gift tax repealed.
22	(3) New tax system.—The Simplified USA
23	Tax consists of—
24	(A) a simplified tax collected from individ-
25	uals, that for years after 1998 replaces the in-

1	come tax imposed on individuals by section 1 of
2	the Code, and
3	(B) a simplified tax collected from corpora-
4	tions and other businesses, that for years after
5	1998 replaces the income tax imposed on cor-
6	porations by section 11 of the Code.
7	(3) SIMPLIFIED USA TAX ON GROSS PROFITS.—
8	Corporations and other businesses pay tax on their
9	annual gross profits from business conducted in the
10	United States, except that—
11	(A) export revenues are excluded, and
12	(B) imports are taxed.
13	(4) SIMPLIFIED USA TAX ON INCOME.—Individ-
14	uals pay tax on their annual income from wages,
15	dividends, interest, and other financial income (in-
16	cluding sales of property), except that—
17	(A) investment earnings on previously
18	taxed income that is placed in a Roth IRA is
19	exempt from further taxation,
20	(B) a portion of each family's income is ex-
21	empt from tax, and
22	(C) deductions are allowed for—
23	(i) education costs,
24	(ii) religious, charitable, and other
25	philanthropic donations,

1	(iii) home mortgage interest pay-
2	ments, and
3	(iv) contributions to qualified IRAs.
4	(5) Credit for fica payroll taxes paid.—
5	The amount of tax due is reduced by the payroll tax
6	that is—
7	(A) in the case of an employee, withheld
8	from wages, or
9	(B) in the case of a corporation or other
10	business, paid by the employer.
11	(c) Concepts and Structure of New Tax Sys-
12	TEM.—
13	(1) Guiding principles of the simplified
14	USA TAX SYSTEM.—The Simplified USA Tax is
15	based on the following principles:
16	(A) National wealth and well-being depend
17	on the work, skill, and savings and investment
18	of people.
19	(B) Businesses are people and their capital
20	working together.
21	(C) Capital makes people more productive.
22	(D) Everyone benefits from a growing
23	stock of national savings which in turn allows
24	for a growing stock of physical and human cap-
25	ital.

1	(E) Under the Simplified USA Tax, the
2	deferral of taxation on investments in human
3	capital represents an investment by the Federal
4	government in the nation's capital stock and
5	the Federal government shares in the return on
6	its investment in the form of higher economic
7	output and revenues in the future.
8	(2) SINGLE TAX IN 2 PARTS.—The Simplified
9	USA Tax is composed of a business tax and an indi-
10	vidual tax which are 2 parts of a single tax system
11	that subjects all income produced and received to
12	taxation once and only once. The 2 parts are as fol-
13	lows:
14	(A) Business tax at the source of in-
15	COME.—Tax is paid by corporations and other
16	businesses which produce and sell goods and
17	services that are—
18	(i) the source of nearly all the gross
19	domestic product of the United States, and
20	(ii) the ultimate source of income re-
21	ceived by individuals.
22	(B) Individual tax on income re-
23	CEIVED.—Tax is paid by individuals when they
24	receive wages and salaries as compensation for

gross domestic product created by their work.

1	(3) Saving and investment.—The Simplified
2	USA Tax allows people to save and businesses to in-
3	vest as follows:
4	(A) Fair opportunity for people to
5	SAVE.—
6	(i) OPTIONAL ELIMINATION OF DOU-
7	BLE TAXATION.—When an individual earns
8	income and is taxed on that income, the
9	individual can save that income in a Roth
10	IRA and not pay income taxes on the in-
11	vestment earnings.
12	(ii) Deductible and excludable
13	SAVINGS.—The Simplified USA Tax con-
14	tinues provisions of present law that
15	allow—
16	(I) lower income individuals and
17	certain other to make deductible con-
18	tributions to individual retirement ac-
19	counts, and
20	(II) encourage employer spon-
21	sored savings and retirement plans
22	that defer taxation of income through
23	use of 401(k) plans and other quali-
24	fied retirement plans.

1	(B) Fair opportunity for businesses
2	TO INVEST.—
3	(i) No prepayment of tax.—When
4	a business invests in plant and
5	equipment—
6	(I) a deduction is allowed for the
7	cost, and
8	(II) tax is deferred.
9	(ii) Tax on earnings and recovery
10	OF COST.—When recovered out of business
11	revenues, both the cost of the investment
12	and the earnings on the investment are in-
13	cluded in gross profit subject to tax.
14	(iii) Expensing.—The deduction for
15	investment is the equivalent of allowing the
16	cost of plant and equipment to be expensed
17	instead of depreciated.
18	(4) Fair opportunity to compete in the
19	GLOBAL MARKETPLACE.—The Simplified USA Tax
20	serves the strategic interests of the United States in
21	international markets as follows:
22	(A) Border adjustable tax.—
23	(i) American-made exports.—
24	Goods and services produced in the United

1	States can be sold into world markets free
2	of tax.
3	(ii) Foreign-made imports.—Goods
4	and services imported into the United
5	States bear a fair and proportionate share
6	of the tax burden in the United States.
7	(iii) Leveling the international
8	PLAYING FIELD.—Border adjustments for
9	exports and imports are consistent with
10	international standards and practice.
11	(5) A SIMPLE AND UNDERSTANDABLE TAX—
12	The Simplified USA Tax for individuals—
13	(A) is written in a simple, understandable
14	form,
15	(B) contains only a few exemptions, deduc-
16	tions, and credits, and can be reported on a tax
17	return only a small fraction the size of Form
18	1040.
19	(6) A nonintrusive, evenhanded tax.—
20	(A) TAXPAYERS ARE IN CONTROL.—When
21	the rules are few and clear, taxpayers can cal-
22	culate their own tax correctly and file their own
23	returns without fear of mistake or of getting
24	caught up in an argument with the IRS.

1	(B) LIMITED ROLE FOR IRS.—When the
2	rules are few and clear, the IRS does not have
3	the broad interpretive power that puts tax-
4	payers at risk of being treated unfairly and un-
5	evenly.
6	(C) RESTORING VOLUNTARY COMPLI-
7	ANCE.—When the rules are few and clear, the
8	IRS can concentrate on helping taxpayers vol-
9	untarily pay their correct share of tax revenues
10	for public use and benefit under a tax system
11	that is understood and respected.
12	(7) Maintaining tax progressivity for in-
13	DIVIDUALS.—
14	(A) Graduated tax.—Like the tax im-
15	posed by section 1 of the current Code, the
16	Simplified USA Tax for individuals is a grad-
17	uated tax.
18	(B) Family Living allowance.—The

(B) Family Living allowance.—The Simplified USA Tax recognizes that every family's budget includes necessities. The Simplified USA Tax provides a family living allowance that exempts from taxation the first dollars earned and spent to maintain a basic standard of living.

1	(8) Businesses and individual share the
2	TAX BURDEN.—
3	(A) Business portion of tax bur-
4	DEN.—Corporations and other businesses pay
5	about the same portion of the total tax as
6	under the current Code.
7	(B) Individual portion of tax bur-
8	DEN.—Individuals pay about the same portion
9	of the total tax as under the current Code.
10	(9) Emphasizing personal independence
11	AND RESPONSIBILITY.—
12	(A) Reinforcing a culture of work
13	AND THRIFT.—Instead of being solely a calcula-
14	tion of how much they must pay to the govern-
15	ment, the Simplified USA Tax converts the in-
16	come tax into an annual calculation of how
17	much people produce and contribute to the
18	economy.
19	(B) Greater control and responsibil-
20	ITY.—Because people are not double taxed on
21	their saving, they have—
22	(i) more control over their own income
23	and taxes,
24	(ii) a greater ability to plan and pro-
25	vide for their own future, and

1	(iii) a fair opportunity to do so.
2	(10) More opportunity for wage earners
3	AT LOWER INCOME LEVELS.—
4	(A) Refundable credit for employee
5	PAYROLL TAX.—The amount of the payroll tax
6	paid or withheld under the Code from an em-
7	ployee's wages (and paid into the Social Secu-
8	rity and Hospital Insurance Trust Funds) is—
9	(i) credited against the employee's in-
10	come tax, and
11	(ii) refunded to the employee to the
12	extent in excess of the employee's income
13	tax.
14	(B) No effect on trust fund or ben-
15	EFITS.—The income tax credit allowed for pay-
16	roll taxes deposited in the Social Security Trust
17	Fund does not—
18	(i) reduce the amount in such fund, or
19	(ii) reduce the payment of any per-
20	son's benefits from the fund.
21	TITLE II—SIMPLIFIED USA TAX
22	FOR INDIVIDUALS
23	SEC. 201. SIMPLIFIED USA TAX FOR INDIVIDUALS.
24	(a) In General.—Chapter 1 of the Code is amended
25	to read as follows:

1 "CHAPTER 1—SIMPLIFIED USA TAX FOR

2 **INDIVIDUALS**

- "Subchapter A. Basic rules.
- "Subchapter B. Roth IRA and other savings provisions.
- "Subchapter C. Basis, business transactions, and nonrecognition transactions.
- "Subchapter D. Rules for exclusions from gross income.
- "Subchapter E. Rules relating to deductions.
- "Subchapter F. Special business activities.
- "Subchapter G. Accounting methods.
- "Subchapter H. Nonresident aliens.
- "Subchapter I. Trusts and estates.
- "Subchapter J. Definitions and rules of application.

3 "Subchapter A—Basic Rules

- "Sec. 1. Simplified USA tax for individuals.
- "Sec. 2. Persons liable for the Simplified USA for individuals.
- "Sec. 3. Gross income.
- "Sec. 4. Exclusions from gross income.
- "Sec. 5. Alimony and child support deductions.
- "Sec. 6. Personal and dependency deduction.
- "Sec. 7. Family Living Allowance.
- "Sec. 8. USA deductions.
- "Sec. 9. Homeowner deduction.
- "Sec. 10. Education deduction.
- "Sec. 11. Philanthropic transfer deduction.
- "Sec. 13. Limitation on deductions.
- "Sec. 15. Tax rates.
- "Sec. 16. Kiddie tax.
- "Sec. 17. Rules for filing status and rate tables.
- "Sec. 20. USA tax credits.
- "Sec. 21. Payroll tax credit.
- "Sec. 22. Taxes-paid tax credit.
- "Sec. 23. Indexing for inflation.

4 "SEC. 1. SIMPLIFIED USA TAX FOR INDIVIDUALS.

- 5 "(a) Imposition of Tax.—An income tax is imposed
- 6 on each individual described in section 2. The income tax
- 7 shall equal the amount determined by applying the tax
- 8 schedules in section 15 to the taxable income of the tax-
- 9 payer for the taxable year and reducing the tax so deter-
- 10 mined by the USA tax credits for the taxable year.

1	"(b) Taxable Income.—'Taxable income' means
2	adjusted gross income, reduced by—
3	"(1) the personal and dependency deduction,
4	"(2) the Family Living Allowance, and
5	"(3) the USA deductions, including—
6	"(A) the homeowner deduction,
7	"(B) the education deduction, and
8	"(C) the philanthropic transfer deduction.
9	"(c) Adjusted Gross Income.—'Adjusted gross in-
10	come' means gross income, reduced by—
11	"(1) the alimony and child support deductions,
12	and
13	"(2) the qualified IRA deduction.
14	"(d) Name.—The tax imposed by this chapter shall
15	be known as the 'Simplified USA Tax for Individuals'.
16	"SEC. 2. PERSONS LIABLE FOR THE SIMPLIFIED USA TAX
17	FOR INDIVIDUALS.
18	"(a) Individuals Only.—The Simplified USA Tax
19	for Individuals shall apply only to individuals.
20	"(b) CITIZENS AND RESIDENT ALIENS.—The Sim-
21	plified USA Tax for Individuals shall apply to all citizens
22	of the United States and to all resident aliens of the
23	United States. Except as specifically provided in this chap-
24	ter, the Simplified USA Tax for Individuals shall not
25	apply to nonresident aliens.

1 "(c) Nonresident Aliens.—For rules applicable to the compensation income of nonresident aliens, see subchapter H (sections 131 and 132). For rules on the with-3 holding of tax on nonresident aliens, see chapter 5 (sections 1441–1464). "(d) TAXPAYER.—For purposes of this chapter, 'tax-6 payer' means an individual, or, in the case of a joint return, the husband and the wife. 8 "SEC. 3. GROSS INCOME. 10 "(a) General Definition.—Except as otherwise provided in this chapter, 'gross income for the taxable year' means all income from whatever source derived by a taxpayer during the taxable year, including (but not lim-14 ited to) the following items: "(1) Compensation for services, including (but 15 not limited to)— 16 "(A) salaries, 17 "(B) wages, 18 "(C) commissions, 19 20 "(D) tips, and "(E) distributions from business entities 21 22 (as defined in section 171). 23 "(2) Fringe benefits (except as specifically ex-24 cluded by section 4(a)), including (but not limited 25 to)—

1	"(A) the cost of health, disability, life or
2	other similar insurance paid by an employer if
3	the taxpayer is indirectly or directly the bene-
4	ficiary of the policy or has the right to name
5	the beneficiary of the policy,
6	"(B) employer-paid parking (unless the
7	employee uses the automobile parked in the
8	space regularly on employer business),
9	"(C) employer-paid educational benefits,
10	"(D) employer-paid housing (other than
11	housing provided for the convenience of the em-
12	ployer),
13	"(E) employer-paid meals (other than
14	meals provided for the convenience of the em-
15	ployer or reimbursement for the reasonable cost
16	of meals incurred on overnight travel),
17	"(F) amounts contributed by an employer
18	on behalf of an employee to a group legal serv-
19	ices plan, and
20	"(G) dependent care assistance received
21	from an employer.
22	"(3) Distributions from business entities
23	(as defined in section 171) constituting—
24	"(A) compensation for use of capital, in-
25	cluding interest, or

1	"(B) shares of profits (including divi-
2	dends).
3	"(4) Interest not described in paragraph (3)(A).
4	"(5) Rents.
5	"(6) Royalties.
6	"(7) Alimony, child support, and separate
7	maintenance payments.
8	"(8) Includible social security benefits.
9	"(9) Income from the discharge of indebted-
10	ness.
11	"(10) Gains on the sale or disposition of assets.
12	"(11) Amounts stolen or embezzled.
13	"(12) Distributions from retirement plans and
14	annuities (other than USA Roth IRAs) to the extent
15	not previously included as income, as determined in
16	accordance with section 33.
17	"(13) Amounts received through health, acci-
18	dent or disability insurance to the extent that—
19	"(A) the cost of such insurance was paid
20	by an employer and not included in the employ-
21	ee's taxable income and
22	"(B) such amounts exceed the actual medi-
23	cal expenses incurred and not paid or treated as
24	paid with amounts otherwise excluded from in-
25	come

1	"(b) Definitions.—For purposes of subsection (a)
2	and section 4—
3	"(1) Employer.—'Employer' includes—
4	"(A) in the case of a partner who provides
5	services for a partnership, the partnership,
6	"(B) in the case of a proprietor, the pro-
7	prietorship, and
8	"(C) in the case of an independent con-
9	tractor, any business or individual that hires
10	the independent contractor.
11	"(2) Social security benefits.—
12	"(A) In general.—'Social Security bene-
13	fits' means any amount received by the tax-
14	payer by reason of entitlement to—
15	"(i) a monthly benefit under title II of
16	the Social Security Act, or
17	"(ii) a tier 1 railroad retirement bene-
18	fit. The amount received by a taxpayer
19	shall be determined as if the Social Secu-
20	rity Act did not contain section 203(i)
21	thereof.
22	"(B) Tier 1 railroad retirement ben-
23	EFIT.—'Tier 1 railroad retirement benefit'
24	means—

1	"(i) the amount of the annuity under
2	the Railroad Retirement Act of 1974 equal
3	to the amount of the benefit to which the
4	taxpayer would have been entitled under
5	the Social Security Act if all of the service
6	after December 31, 1936, of the employee
7	(on whose record the annuity is being
8	paid) has been included in the term 'em-
9	ployment' as defined in the Social Security
10	Act, and
11	"(ii) a monthly annuity amount under
12	section 3(f)(3) of the Railroad Retirement
13	Act of 1974.
14	"(C) Workers' compensation sub-
15	STITUTES.—If by reason of section 224 of the
16	Social Security Act or section 3(a)(1) of the
17	Railroad Retirement Act of 1974, any social se-
18	curity benefit is reduced because of the receipt
19	of a benefit under a workers' compensation act,
20	the term 'social security benefit' includes that
21	portion of such benefit which equals such reduc-
22	tion.
23	"(D) Effect of Early Payment.—If so-
24	cial security benefits checks are delivered before

the end of the calendar month for which they

are issued and are not deposited until the month for which they are issued, they will be treated as received in the month for which they are issued.

"(3) Includible social security benefits' means the portion of social security benefits that would be included in gross income under section 86(a) of the Internal Revenue Code of 1986, except that for purposes of applying such section, the term 'modified adjusted gross income' means adjusted gross income (as defined in section 1(c)), determined without regard to the inclusion of any social security benefits. "(c) Property Received for Services.—

"(1) IN GENERAL.—If, in connection with the performance of services, property is transferred to any person other than the person for whom such services are performed, the excess of—

"(A) the fair market value of such property (determined without regard to any restriction other than a restriction which by its terms will never lapse) at the first time the rights of the person having the beneficial interest in such property are transferable or are not subject to

1 a substantial risk of forfeiture, whichever oc-2 curs earlier, over

"(B) the amount (if any) paid for such property, shall be included in the gross income of the person who performed such services in the first taxable year in which the rights of the person having the beneficial interest in such property are transferable or are not subject to a substantial risk of forfeiture, whichever is applicable. The preceding sentence shall not apply if such person sells or otherwise disposes of such property in an arm's length transaction before his rights in such property become transferable or not subject to a substantial risk of forfeiture.

"(2) Rules and regulations.—The Secretary shall prescribe rules and regulations similar to those applicable under section 83 of the Internal Revenue Code of 1986 for purposes of implementing this subsection.

21 "SEC. 4. EXCLUSIONS FROM GROSS INCOME.

- 22 "(a) GENERAL RULE.—Gross income does not in-23 clude:
- 24 "(1) Returns or benefits from pre-25 Viously taxed income.—

1	"(A) Social security benefits (as defined in
2	section 3(b)(2)), other than includible social se-
3	curity benefits (as defined in section 3(b)(3)).
4	"(B) Amounts received under accident or
5	health benefit plans (except as provided in sec-
6	tion $3(a)(13)$).
7	"(C) Value of services provided pursuant
8	to a group legal service plan (but only if the
9	cost of such services was paid by the employee
10	or paid by the employer and included in the
11	gross income of the employee).
12	"(D) Amounts received under an insurance
13	contract for certain living expenses in the case
14	of an individual whose principal residence is
15	damaged or destroyed or who is denied access
16	because of the threat of such occurrence.
17	"(E) Amounts treated as recovery of basis
18	under any other provision of chapter 1.
19	"(2) Compensation for special kinds of
20	SERVICE.—
21	"(A) In the case of a minister of the
22	gospel—
23	"(i) the rental value of a home fur-
24	nished to him, or

1	"(ii) the rental allowance paid to him
2	as part of his compensation, to the extent
3	used by him to rent or provide a home.
4	"(B) Certain combat pay of members of
5	the Armed Forces of the United States (as pro-
6	vided in section 92).
7	"(C) Certain reduced uniform services re-
8	tirement pay (as defined in section 122 of the
9	Internal Revenue Code of 1986).
10	"(D) Qualified military benefits (as defined
11	in section 93).
12	"(E) Moving allowances for active military
13	personnel (as defined in section 217(g) of the
14	Internal Revenue Code of 1986).
15	"(F) Certain foster care payments (as de-
16	fined in section 94).
17	"(3) Gratuitous, Charitable, and Govern-
18	MENTAL TRANSFERS.—
19	"(A) Gifts.
20	"(B) Inheritances.
21	"(C) Supplemental security income, aid to
22	families with dependent children, food stamps,
23	section 8 low-income rental assistance, benefits
24	under the low-income home energy assistance
25	program, and benefits under other similar Fed-

1	eral and State assistance programs for low-in-
2	come individuals and families.
3	"(D) Benefits or assistance received from
4	a charitable organization as the result of a dis-
5	aster or by reason of financial need.
6	"(4) Tax-exempt bond interest.—Interest
7	on State and local bonds (as provided in section 91);
8	"(5) Compensation for injury and sick-
9	NESS.—
10	"(A) Amounts received as compensation
11	for personal injury or sickness (as provided in
12	section 95).
13	"(B) Reimbursement and direct payments
14	under Medicare and Medicaid.
15	"(6) Benefits primarily for the conven-
16	IENCE OF THE EMPLOYER AND CERTAIN FRINGE
17	BENEFITS.—
18	"(A) Meals or lodging furnished for the
19	convenience of the employer (as provided in sec-
20	tion 96).
21	"(B) Value of a parking space if employee
22	uses the car parked in the space regularly on
23	company business.
24	"(C) A fringe benefit that is a no-addi-
25	tional-cost service (as defined in section 97(b)).

1	subject to rules prohibiting discrimination in
2	favor of the highly compensated.
3	"(D) A qualified employee discount (as de-
4	fined in section 97(c)), subject to rules prohibit-
5	ing discrimination in favor of the highly com-
6	pensated.
7	"(E) Any property or services provided to
8	an employee to the extent that if the employee
9	were treated as a business and the business
10	paid for those services, the employee could de-
11	duct the cost of such property or services under
12	the business tax.
13	"(F) A de minimis fringe benefit (as de-
14	fined in section 97(d)).
15	"(G) Transportation in a commuter high-
16	way vehicle if such transportation is in connec-
17	tion with travel between the employee's resi-
18	dence and place of employment.
19	"(H) Any amount received directly or indi-
20	rectly by an individual from an employer for
21	moving expenses if—
22	"(i) the move is associated with a
23	change in job locations for the same em-
24	ployer, and

1	"(ii) the expenses of such move would
2	have been deductible under the rules under
3	section 217 of the Internal Revenue Code
4	of 1986 if paid directly by the employee.
5	"(I) Employer provided coverage under an
6	accident or health plan.
7	"(7) Repayable receipts.—The proceeds of
8	borrowing or any other amounts legally received that
9	the taxpayer is legally obligated to return (except
10	that the imputed interest rules of section 7872 may
11	apply if there is inadequate stated interest).
12	"(8) Certain income earned abroad.—Cer-
13	tain income and housing costs of citizens and resi-
14	dents of the United States living outside the United
15	States in accordance with the rules under section
16	911 of the Internal Revenue Code of 1986.
17	"(9) DISCHARGE OF INDEBTEDNESS.—The
18	amount of indebtedness discharged unless the dis-
19	charge is for services, property, or other valuable
20	right.
21	"(10) Nonrecognition transactions.—
22	Amounts to which the nonrecognition transaction
23	rules of section 77 apply.
24	"(11) Proceeds from sale of principal
25	RESIDENCE.—Amounts excludable under section 76

- 1 (relating to certain proceeds from the sale of the 2 taxpayer's principal residence).
- "(12) Taxable receipts of a business entity.—Amounts that are treated as taxable receipts of a business entity under the Simplified USA Tax for businesses and are not distributed to the individual taxpayer.
- 8 "(13) QUALIFIED RETIREMENT CONTRIBU-9 TIONS.—Employer contributions to retirement plans 10 that are exempt from taxation under chapter 3, in-11 cluding contributions pursuant to a cash or deferred 12 payment plan described in section 401(k).
- 13 "(b) Cross References.—
- 14 "(1) ROTH IRAS.—For rules excluding from 15 income earnings on, and distributions from, Roth 16 IRAs, see sections 30 and 408A.
- 17 "(2) OTHER RETIREMENT PLANS.—For rules 18 excluding or deferring from income earnings on 19 other retirement plans, see chapter 3.
- 20 "SEC. 5. ALIMONY AND CHILD SUPPORT DEDUCTIONS.
- "(a) GENERAL RULE.—A taxpayer shall be allowed an alimony and child support deductions for an amount equal to the alimony, child support, or separate maintenance payments paid during the taxpayer's taxable year.

1	"(b) Definition of Alimony, Child Support
2	AND SEPARATE MAINTENANCE PAYMENTS.—'Alimony,
3	child support, and separate maintenance payments' means
4	any alimony, child support, or separate maintenance pay-
5	ment which is includible in gross income of the recipient
6	under section 3.
7	"SEC. 6. PERSONAL AND DEPENDENCY DEDUCTION.
8	"(a) Amount of Exemption.—The personal and
9	dependency deduction for an individual shall equal the
10	number of exemptions multiplied by \$2,700.
11	"(b) Number of Exemptions.—
12	"(1) Taxpayer.—One exemption shall be al-
13	lowed for the taxpayer unless the taxpayer files a
14	joint return with a spouse, in which case 1 exemp-
15	tion shall be allowed for the husband and 1 for the
16	wife.
17	"(2) Eligible Dependent.—An exemption
18	shall be allowed for each eligible dependent.
19	"(c) Dependent.—
20	"(1) Definition.—'Dependent' means any of
21	the following individuals over half of whose support
22	for the calendar year was received from the taxpayer
23	or is treated as received from the taxpayer:
24	"(A) A son or daughter of the taxpayer, or
25	a descendant of either

1	"(B) A stepson, stepdaughter, stepfather,
2	or stepmother of the taxpayer.
3	"(C) A brother, sister, stepbrother, or
4	stepsister of the taxpayer.
5	"(D) The father or mother of the tax payer,
6	or an ancestor of either.
7	"(E) A son or daughter of a brother or sis-
8	ter of the taxpayer.
9	"(F) A brother or sister of the mother or
10	father of the taxpayer.
11	"(G) A son-in-law, daughter-in-law, father-
12	in-law, mother-in-law, brother-in-law, or sister-
13	in-law of the taxpayer.
14	"(H) An individual (other than an individ-
15	ual who at any time during the taxable year
16	was the spouse, determined without regard to
17	section 7703, of a taxpayer) who, for the tax-
18	able year of the taxpayer, has as his principal
19	place of abode the home of the taxpayer and is
20	a member of the taxpayer's household.
21	"(2) Rules relating to the general defi-
22	NITION.—The Secretary shall prescribe rules similar
23	to the rules under section 152 of the Internal Reve-
24	nue Code of 1986 that shall apply to the general
25	definition of 'dependent', including definitional rules,

1	rules relating to multiple support agreements, and
2	support tests in cases of children of divorced par-
3	ents.
4	"(d) Eligible Dependent.—
5	"(1) In general.—'Eligible dependent' means
6	a dependent—
7	"(A) whose gross income for the calendar
8	year in which the taxable year of the taxpayer
9	begins is less than the exemption amount, or
10	"(B) who is a child of the taxpayer and
11	who—
12	"(i) has not attained the age of 19 at
13	the close of the calendar year in which the
14	taxable year of the taxpayer begins, or
15	"(ii) is a student who has not attained
16	the age of 24 at the close of such calendar
17	year.
18	"(2) Exclusions.—A dependent who files a
19	joint return with a spouse for the calendar year is
20	not an eligible dependent.
21	"(3) Rules relating to definitions.—The
22	Secretary shall prescribe rules similar to those in-
23	cluded in or applicable under the Internal Revenue
24	Code of 1986 relating to this subsection, including

- 1 rules defining 'child' and 'student' and rules relating
- 2 to the income of handicapped dependents.
- 3 "(e) Inflation Adjustment.—The dollar amount
- 4 contained in subsection (a) shall be adjusted for inflation
- 5 beginning with calendar year 1999 in accordance with the
- 6 procedures of section 23.

7 "SEC. 7. FAMILY LIVING ALLOWANCE.

- 8 "(a) Amount of Allowance.—The Family Living
- 9 Allowance for a taxpayer shall be determined in accord-
- 10 ance with the following schedule:

Form of Return:	Family Living Allowance:
Taxpayers filing joint return	\$8,140.
Surviving spouse	\$8,140.
Head of household	\$5,940.
Individual who is not married or a	\$4,840.
head of household.	
Married filing separate return	\$4,070.

- 11 "(b) Limitation in the Case of Certain De-
- 12 PENDENTS.—In the case of an individual for whom an-
- 13 other taxpayer can claim an exemption under section 6,
- 14 the Family Living Allowance for such individual shall not
- 15 exceed the greater of \$700 or such individual's earned in-
- 16 come (as defined in section 171(a)(6)).
- 17 "(c) Adjustments for Inflation.—The dollar
- 18 amounts contained in subsections (a) and (b) shall be ad-
- 19 justed for inflation beginning with calendar year 1999 in
- 20 accordance with the procedures of section 23.

1 "SEC. 8. USA DEDUCTIONS.

2	"In computing taxable income, an individual shall be
3	entitled to the following deductions:
4	"(1) The homeowner deduction described in
5	section 9.
6	"(2) The education deduction described in sec-
7	tion 10.
8	"(3) The philanthropic transfer deduction de-
9	scribed in section 11.
10	"SEC. 9. HOMEOWNER DEDUCTION.
11	"(a) In General.—The homeowner deduction shall
12	equal the amount of interest paid by the taxpayer during
13	the taxable year on acquisition indebtedness with respect
14	to any qualified residence of the taxpayer.
15	"(b) Definitions.—
16	"(1) Acquisition indebtedness.—'Acquisi-
17	tion indebtedness' means any indebtedness that is
18	secured by a qualified residence and that—
19	"(A) was incurred in acquiring, construct-
20	ing, or substantially improving the qualified res-
21	idence, or
22	"(B) was incurred to refinance any indebt-
23	edness that is described in subparagraph (A) or
24	this subparagraph (B) but only to the extent
25	that the refinancing does not exceed the
26	amount refinanced.

- The aggregate amount treated as acquisition indebtedness shall not exceed \$1,000,000 (\$500,000 in the case of a married individual filing separately).
- "(2) QUALIFIED RESIDENCE.—'Qualified residence' means the principal residence of the taxpayer and 1 other residence of the taxpayer that is designated by the taxpayer and which—
- 8 "(A) is used by the taxpayer as a residence 9 for more than 14 days during such year for 10 which such unit is rented, and
- 11 "(B) is not rented for more than 14 days 12 during such year.
- 13 "(c) Cooperative Housing Corporation Ten-
- 14 ANT.—Any indebtedness secured by stock held by a tax-
- 15 payer as a tenant-stockholder in a cooperative housing cor-
- 16 poration shall be treated as secured by the house or apart-
- 17 ment which the taxpayer is entitled to occupy as a tenant-
- 18 stockholder. If such stock cannot be used to secure indebt-
- 19 edness, the indebtedness will be treated as so secured if
- 20 the taxpayer establishes that such indebtedness was in-
- 21 curred to acquire stock.
- 22 "SEC. 10. EDUCATION DEDUCTION.
- "(a) In General.—The education deduction shall
- 24 equal the sum of the qualified educational expenses for
- 25 each eligible student.

1	"(b) Qualified Education Expenses.—
2	"(1) In general.—'Qualified education ex-
3	penses' means with respect to an eligible student the
4	lesser of—
5	"(A) \$4,000, or
6	"(B) the qualified higher education ex-
7	penses of the eligible student paid by the tax-
8	payer during the taxable year.
9	"(2) Qualified higher education ex-
10	PENSES.—
11	"(A) IN GENERAL.—'Qualified higher edu-
12	cation expenses' means tuition and fees re-
13	quired for the enrollment of an eligible student
14	at an eligible education institution. Such term
15	shall not include expenses with respect to any
16	course or other education involving sports.
17	games, or hobbies other than as part of a de-
18	gree program.
19	"(B) ELIGIBLE EDUCATIONAL INSTITU-
20	TION.—'Eligible educational institution'
21	means—
22	"(i) an institution which is described
23	in section 481 of the Higher Education
24	Act of 1965 (as in effect on May 15

1	1998), and which is eligible to participate
2	in a program under title IV of such Act.
3	"(ii) in the case of a student who has
4	attained the age of 18 before the beginning
5	of the taxable year, and not graduated
6	from high school before the beginning of
7	the taxable year, an accredited school pro-
8	viding remedial education.
9	"(3) ELIGIBLE STUDENT.—'Eligible student'
10	means—
11	"(A) the taxpayer, but only if no other tax-
12	payer treats the taxpayer as a dependent for
13	which an exemption is allowed in computing the
14	dependency deduction under section 6,
15	"(B) the taxpayer's spouse if a joint return
16	is filed, and
17	"(C) any dependent of the taxpayer for
18	whom the taxpayer is allowed an exemption in
19	computing the dependency deduction under sec-
20	tion 6.
21	"(c) Limitation.—The maximum education deduc-
22	tion in a taxable year is \$12,000 (\$6,000 in the case of
23	married individuals filing separate returns).
24	"(d) Inflation Adjustments.—The dollar
25	amounts contained in subsections (b)(1)(A) and (c) shall

1	be adjusted for inflation beginning with calendar year
2	1999 in accordance with section 23.
3	"SEC. 11. PHILANTHROPIC TRANSFER DEDUCTION.
4	"(a) In General.—The philanthropic transfer de-
5	duction shall equal the amount of charitable contributions
6	made by the taxpayer in the taxable year, subject to the
7	limitations in subsection (b). A deduction shall be allow-
8	able as a deduction only if verified under regulations pre-
9	scribed by the Secretary.
10	"(b) Limitation on Amount.—
11	"(1) General Rule.—A deduction for con-
12	tributions to regular charities in any taxable year
13	shall be allowed only to the extent that such con-
14	tributions do not exceed 50 percent of the taxpayer's
15	adjusted gross income. Other charitable contribu-
16	tions shall be allowed only to the extent that such
17	contributions do not exceed the lesser of—
18	"(A) 30 percent of the taxpayer's adjusted
19	gross income, or
20	"(B) the excess, if any, of 50 percent of
21	the taxpayer's adjusted gross income over the
22	amount of charitable contributions to regular
23	charities.
24	"(2) Carryover.—If the amount of charitable
25	contributions made in a taxable year exceeds the

- amount which can be deducted in such year, the excess shall be carried over for a period of up to 5 years in accordance with rules to be prescribed by the Secretary.
- 5 "(3) REGULAR CHARITY.—For purposes of this 6 subsection, 'regular charity' means an organization 7 described in section 101, that is not a private foun-8 dation (other than a private operating foundation) 9 (as such terms are defined in section 102).
- "(c) Charitable Contribution.—'Charitable contribution' means a contribution or gift to or for the use of a governmental or charitable recipient (as defined in section 101).
- 14 "(d) Contributions of Property.—
- 15 "(1) GENERAL RULE.—In the case of a chari-16 table contribution of property, the amount of the 17 contribution shall equal the lesser of the fair market 18 value of the property or the taxpayer's basis in the 19 property.
 - "(2) Fair market value deductions in Certain cases.—Notwithstanding paragraph (1), in the case of a charitable contribution (other than a contribution to a private foundation that is not a private operating foundation) of—
- 25 "(A) real property,

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1	"(B) tangible property if the use by the
2	donee is related to its purpose or function con-
3	stituting the basis for its exemption from the
4	business tax or in the case of a governmental
5	unit, to any governmental unit, and
6	"(C) stocks, bonds, or other securities held
7	for more than one year,
8	the amount of the charitable contribution shall equal
9	the fair market value of the property.
10	"(3) Contributions of Stock for which
11	MARKET QUOTATIONS ARE READILY AVAILABLE.—
12	"(A) IN GENERAL.—In the case of con-
13	tributions of qualified appreciated stock, para-
14	graph (2) shall apply without regard to whether
15	the stock is contributed to a private foundation.
16	"(B) Qualified appreciated stock.—
17	'Qualified appreciated stock' means any stock
18	of a corporation for which (as of the date of the
19	contribution) market quotations are readily
20	available on an established securities market,
21	except that in the case of a donor to a private
22	foundation, the term does not include stock to
23	the extent that the amount so contributed,
24	when increased by prior contributions by the
25	donor of stock in the same corporation, exceeds

1	10 percent in value of the outstanding stock of
2	such corporation.
3	"(e) Other Rules.—The Secretary shall prescribe
4	rules limiting the availability of the philanthropic transfer
5	deduction in certain cases, including rules for—
6	"(1) contributions of property placed in trust,
7	"(2) contributions of partial interests in prop-
8	erty,
9	"(3) contributions subject to liabilities that are
10	assumed,
11	"(4) out-of-pocket expenditures on behalf of a
12	charity to influence legislation,
13	"(5) substantiation of contributions in excess of
14	\$250,
15	"(6) contributions designated for lobbying activ-
16	ity,
17	"(7) amounts paid to maintain certain students
18	as members of taxpayer's household,
19	"(8) qualified conservation contributions, and
20	"(9) deductions for travel expenses on behalf of
21	a charity where there is a significant element of per-
22	sonal pleasure.
23	"SEC. 13. LIMITATION ON DEDUCTIONS.
24	"(a) IN GENERAL.—A taxpayer's deductions shall not
25	reduce the taxpayer's taxable income below zero. Except

1	as provided in section 11(b) (relating to the limitation on		
2	the philanthropic transfer deduction), a taxpayer shall not		
3	be entitled to carry over any unused deductions.		
4	"(b) Deductions.—For purposes of this section,		
5	'deductions' means—		
6	"(1) the alimony and child support deductions,		
7	"(2) the personal and dependency deduction,		
8	"(3) the Family Living Allowance,		
9	"(4) the USA deductions, and		
10	"(5) the qualified IRA deduction.		
11	"SEC. 15. TAX RATES.		
12	"(a) Married Individuals Filing Joint Returns		
13	AND SURVIVING SPOUSES.—The tax schedule for every		
14	married individual who files a joint return with a spouse		
15	and for every surviving spouse (as defined in section		
16	17(a)) is— "If taxable income is: Not over \$40,000		
17	"(b) Heads of Households.—The tax schedule for		
18	every head of household (as defined in section 17(b)) is— "If taxable income is: Not over \$35,000		

- 1 "(c) Unmarried Individuals.—The tax schedule
- 2 for an unmarried individual who is not a head of a house-
- 3 hold or a surviving spouse is—

If taxable income is:				
Not or	ver \$24,000			
Over	\$24,000,	but	not	over
\$48	,000.			
Over 8	\$48,000			

The tax is:

15% of taxable income.

\$3,600, plus 25% of the excess over \$24,000.

\$9,600, plus 30% of the excess over \$48,000.

- 4 "(d) Married Individuals Filing Separate Re-
- 5 TURNS.—The tax schedule for a married individual filing
- 6 a separate return is—

"If taxable income is: Not over \$20,000 Over \$20,000, but not over \$40,000. Over \$40,000

The tax is:

15% of taxable income.

\$3,000, plus 25% of the excess over \$20,000.

\$8,000, plus 30% of the excess over \$40,000.

- 7 "(e) Adjustments for Inflation.—Beginning
- 8 with calendar year 1999, the tax schedules in subsections
- 9 (a) through (d) shall be adjusted so that inflation will not
- 10 result in tax increases in accordance with the procedures
- 11 under section 23.
- 12 "(f) Definitions.—See section 17 for rules on filing
- 13 status.
- 14 "SEC. 16. KIDDIE TAX.
- 15 "(a) GENERAL RULE.—If a child has a living parent
- 16 and net unearned income and the child has not attained
- 17 the age of 14 before the close of the taxable year—
- "(1) the net unearned income of the child shall
- be included in the taxable income of the eligible par-

1	ent for purposes of determining the parent's tax li-
2	ability, or
3	"(2) the tax calculated under the tax rate
4	schedules for the child as a separate taxpayer shall
5	not be less than the sum of—
6	"(A) the tax which would have been deter-
7	mined under the rate schedule if the taxable in-
8	come of the child were reduced by the net un-
9	earned income of the child, plus
10	"(B) such child's share of the allocable pa-
11	rental tax.
12	"(b) Child's Share of Allocable Parental
13	Tax.—
14	"(1) Allocable Parental Tax.—'Allocable
15	parental tax' means the excess of—
16	"(A) the tax that would have been deter-
17	mined under the rate schedules on the eligible
18	parent's taxable income if such income included
19	the net unearned income of all of the eligible
20	parent's children to which this section applies,
21	over
22	"(B) the tax actually determined under the
23	rate schedules without regard to this section.
24	"(2) Child's share of the
25	allocable parental tax is equal to the amount that

1	bears the same ratio to the total allocable parental
2	tax as the child's net unearned income bears to the
3	aggregate net unearned income of all children to
4	whom this section applies for whom the eligible par-
5	ent is the eligible parent.
6	"(c) Eligible Parent.—'Eligible parent' means—
7	"(1) both parents of the child if the parents file
8	a joint return,
9	"(2) the surviving parent of a child if the child
10	has only 1 surviving parent,
11	"(3) the custodial parent if the child's parents
12	are not married, or
13	"(4) the parent with the greater taxable income
14	if the parents are married and filing separate re-
15	turns.
16	"(d) Net Unearned Income.—'Net unearned in-
17	come' means the excess, if any, of—
18	"(1) the adjusted gross income of the child,
19	over
20	"(2) the sum of—
21	"(A) the earned income (as defined in sec-
22	tion $171(a)(6)$) of the child, and
23	"(B) an amount equal to the Family Liv-
24	ing Allowance for a dependent child.

$1\,\,$ "sec. 17. Rules for filing status and rate tables.

2	"(a) Definition of Surviving Spouse.—
3	"(1) In general.—'Surviving spouse' means
4	an individual—
5	"(A) whose spouse died during either of
6	his 2 calendar years immediately preceding the
7	calendar year, and
8	"(B) who maintains as his home a house-
9	hold which constitutes for the taxable year the
10	principal place of abode (as a member of such
11	household) of a dependent—
12	"(i) who (within the meaning of sec-
13	tion 6) is a son, stepson, daughter, or step-
14	daughter of the taxpayer, and
15	"(ii) who the taxpayer is entitled to
16	treat as an exemption for purposes of com-
17	puting the personal dependency deduction
18	for the taxable year under section 6.
19	For purposes of this paragraph, an individual shall
20	be considered as maintaining a household only if
21	over half of the cost of maintaining the household
22	during the taxable year is furnished by such individ-
23	ual.
24	"(2) Limitations.—Notwithstanding para-
25	graph (1), for purposes of section 15, an individual
26	shall not be considered to be a surviving spouse—

1	"(A) if the individual has remarried at any
2	time before the close of the taxable year, or
3	"(B) unless, for the individual's taxable
4	year during which his spouse died, a joint re-
5	turn could have been made under the provisions
6	of section 6013 (without regard to subsection
7	(a)(3) thereof).
8	"(3) Special rule where deceased spouse
9	WAS IN MISSING STATUS.—If an individual was in a
10	missing status (within the meaning of section
11	6013(f)(3)) as a result of service in a combat zone
12	and if such individual remains in such status until
13	the date referred to in subparagraph (A) or (B),
14	then, for purposes of paragraph (1)(A), the date on
15	which such individual died shall be treated as the
16	earlier of the date determined under subparagraph
17	(A) or the date determined under subparagraph (B):
18	"(A) the date on which the determination
19	is made under section 556 of title 37 of the
20	United States Code or under section 5566 of
21	title 5 of such Code (whichever is applicable)
22	that such individual died while in such missing
23	status, or
24	"(B) the date which is 2 years after the
25	date designated under section 92 (relating to

1 exemption for combat zones) as the date of ter-2 mination of combatant activities in that zone. 3 "(b) DEFINITION OF HEAD OF HOUSEHOLD.— "(1) IN GENERAL.—An individual shall be con-4 5 sidered a head of a household if, and only if, such 6 individual is not married at the close of his taxable 7 year, is not a surviving spouse (as defined in sub-8 section (a)), and either— "(A) maintains as his home a household 9 which constitutes for more than one-half of 10 11 such taxable year the principal place of abode, 12 as a member of such household, of— 13 "(i) a son, stepson, daughter, or step-14 daughter of the taxpaver, or a descendant 15 of a son or daughter of the taxpayer, but 16 if such son, stepson, daughter, step-17 daughter, or descendant is married at the 18 close of the taxpayer's taxable year, only if 19 the taxpayer is entitled to claim such per-20 son as an exemption for the taxable year 21 for purposes of computing the dependency 22 deduction under section 6 (or would be so 23 entitled but for the release of a claim to 24 such exemption by the custodial parent),

1	"(ii) any other person who is a de-
2	pendent of the taxpayer, if the taxpayer is
3	entitled to claim such person as an exemp-
4	tion in determining the personal depend-
5	ency deduction for the taxable year, or
6	"(B) maintains a household which con-
7	stitutes for such taxable year the principal place
8	of abode of the father or mother of the tax-
9	payer, if the taxpayer is entitled to a personal
10	dependency deduction for the taxable year for
11	such father or mother.
12	For purposes of this paragraph, an individual shall
13	be considered as maintaining a household only if
14	over half of the cost of maintaining the household
15	during the taxable year is furnished by such individ-
16	ual.
17	"(2) Determination of status.—For pur-
18	poses of this subsection—
19	"(A) a legally adopted child of a person
20	shall be considered a child of such person by
21	blood;
22	"(B) an individual who is legally separated
23	from his spouse under a decree of divorce or of
24	separate maintenance shall not be considered as
25	married;

1	"(C) a taxpayer shall be considered as not
2	married at the close of his taxable year if at
3	any time during the taxable year his spouse is
4	a nonresident alien; and
5	"(D) a taxpayer shall be considered as
6	married at the close of his taxable year if his
7	spouse (other than a spouse described in sub-
8	paragraph (C)) died during the taxable year.
9	"(3) Limitations.—Notwithstanding para-
10	graph (1), for purposes of this chapter, a taxpayer
11	shall not be considered to be a head of a
12	household—
13	"(A) if at any time during the taxable year
14	he is a nonresident alien; or
15	"(B) by reason of an individual who would
16	not be a dependent for the taxable year but
17	for—
18	"(i) subparagraph (H) of section
19	6(e)(1) or
20	"(ii) multiple support rules prescribed
21	by the Secretary.
22	"(c) Certain Married Individuals Living
23	APART.—For purposes of this part, an individual shall be
24	treated as not married at the close of the taxable year

- 1 if such individual is so treated under the provisions of sec-
- 2 tion 7703(b).
- 3 "(d) Nonresident Aliens.—In the case of a non-
- 4 resident alien individual, the taxes imposed by section 1
- 5 shall not apply.
- 6 "SEC. 20. USA TAX CREDITS.
- 7 "(a) IN GENERAL.—The USA tax credits are and
- 8 shall be applied in the following order:
- 9 "(1) The foreign tax credit as prescribed by the
- 10 Secretary under rules similar to the rules of subpart
- 11 A of part III of subchapter N of chapter 1 of the
- 12 Internal Revenue Code of 1986, but only with re-
- spect to foreign taxes on amounts that are included
- in the gross income of the taxpayer.
- 15 "(2) The payroll tax credit under section 21.
- 16 "(3) The taxes-paid tax credit under section 22.
- 17 "(b) Refundable Credits.—If a taxpayer's USA
- 18 tax credits (other than the foreign tax credit) for a taxable
- 19 year exceed the taxpayer's tax liability for the taxable year
- 20 (after application of the foreign tax credit but before appli-
- 21 cation of the other USA tax credits), the taxpayer shall
- 22 be entitled to a refund for such excess. The taxpayer may
- 23 elect in lieu of a refund to apply such excess as a tax paid
- 24 for the following taxable year.

1 "SEC. 21. PAYROLL TAX CREDIT.

2	"(a) In General.—A taxpayer shall be allowed a
3	payroll tax credit in an amount equal to the sum of—
4	"(1) the employee's share of the basic FICA
5	tax,
6	"(2) the employee's share of the basic Tier 1
7	railroad retirement tax, and
8	"(3) one-half of the basic SECA tax payable
9	with respect to the taxpayer's compensation or earn-
10	ings during the taxable year.
11	"(b) Definitions.—
12	"(1) Employee's share of the basic fica
13	TAX.—'Employee's share of the basic FICA tax'
14	means the old-age, survivors and disability insurance
15	tax imposed by section 3101(a) and the portion of
16	the hospital insurance tax imposed by section
17	3101(b) that is attributable to the wage base on
18	which the section 3101(a) tax is imposed.
19	"(2) Employee's share of the basic tier 1
20	RAILROAD RETIREMENT TAX.—Employee's share of
21	the basic Tier 1 railroad retirement tax' means—
22	"(A) the portion of the tax imposed by sec-
23	tion 3201 with respect to compensation below
24	the applicable base (as defined in section
25	3231(e)(2); and

1 "(B) the portion of the tax imposed by sec2 tion 3211(a)(1) on railroad employee represent3 atives attributable to the tax imposed by section
4 3101(a) and the portion of the hospital insur5 ance tax imposed by section 3101(b) that is at6 tributable to the wage base on which the section
7 3101(a) tax is imposed.

"(3) Basic seca tax.—'Basic Seca tax' 8 9 means the old-age, survivors and disability insurance 10 tax imposed by section 1401(a) on self-employment 11 income and the portion of the hospital insurance tax 12 imposed by section 1401(b) on self-employment in-13 come that is attributable to the amount of self-em-14 ployment income (as determined under section 15 1402(b)) on which the section 1401(a) tax is im-16 posed.

"(c) No Credit for Refundable Tax.—No credit
shall be allowed with respect to any FICA tax or railroad
retirement tax for which a taxpayer is entitled to a refund
because of overpayment of tax on the applicable wage
base.

22 "SEC. 22. TAXES-PAID TAX CREDIT.

23 "The taxes-paid tax credit shall equal the sum of—
24 "(1) WAGE WITHHOLDING.—The amount with25 held as tax under chapter 24.

- 1 "(2) Special refunds of social security 2 TAX WHEN WAGES EARNED FROM MORE THAN 1 EM-3 PLOYER.—The amount allowable under section 4 6413(c) as a special refund of taxes imposed on 5 wages. "(3) Overpayments of prior-year tax.— 6 7 Any overpayment of a prior tax obligation that the 8 taxpayer or the Secretary applies to the tax for the 9 taxable year. 10 "(4) Estimated taxes.—Any estimated taxes 11 paid by the taxpayer with respect to the taxpayer's 12 tax liability for the taxable year which are treated as 13 payment on account of income tax for purposes of 14 section 6315 (relating to estimated taxes). 15 "SEC. 23. INDEXING FOR INFLATION. 16 "(a) Publication of Tables and Numbers.—Not later than December 15 of 1998, and each subsequent cal-18 endar year, the Secretary shall prescribe tables and dollar 19 amounts which shall apply in the immediately following 20 calendar year in lieu of the tables and dollar amounts that 21 are required to be adjusted for inflation in accordance with 22 this section. 23 "(b) Method of Adjustment.—
- 24 "(1) IN GENERAL.—The dollar amounts which 25 are required to be adjusted pursuant to this section

for a calendar year shall be the dollar amounts as stated in this chapter multiplied by the cost of living adjustment for such calendar year, rounded as provided in subsection (d).

"(2) Tax rate tables.—In the case of a tax rate table, the dollar amounts to be adjusted in accordance with paragraph (1) are the minimum and maximum dollar amounts for each rate bracket for which a tax is imposed. The amounts setting forth the bottom tax for each bracket shall be adjusted to the extent necessary to reflect the adjustments in the rate brackets.

"(c) Cost-of-Living Adjustment.—

- "(1) IN GENERAL.—The cost-of-living adjustment for any calendar year is the percentage (if any) by which—
- 17 "(A) the CPI for the preceding calendar 18 year, exceeds
- 19 "(B) the CPI for the calendar year 1997.
- "(2) CPI FOR ANY CALENDAR YEAR.—For purposes of paragraph (1), the CPI for any calendar year is the average of the Consumer Price Index as of the close of the 12-month period ending on August 31 of such calendar year.

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1	"(3) Consumer price index.—For purposes
2	of paragraph (2), 'Consumer Price Index' means the
3	last Consumer Price Index for all-urban consumers
4	published by the Department of Labor. For pur-
5	poses of the preceding sentence, the revision of the
6	Consumer Price Index which is most consistent with
7	the Consumer Price Index for calendar year 1998
8	shall be used.
9	"(d) Rounding.—
10	"(1) In general.—If any increase determined
11	under subsection (b) is not a multiple of \$50, such
12	increase shall be rounded to the next lowest multiple
13	of \$50.
14	"(2) Multiples of \$25.—Paragraph (1) shall
15	be applied by substituting '\$25' for '\$50' in the case
16	of—
17	"(A) amounts for married individuals filing
18	separately, and
19	"(B) any other dollar amount that is to be
20	adjusted for inflation if that dollar amount is
21	less than \$1,000.
22	"Subchapter B—Roth IRA and Other Savings
23	Provisions

[&]quot;Sec. 30. Roth IRAs.

[&]quot;Sec. 31. Deductible IRAs. $\,$

[&]quot;Sec. 32. Effect of repeal of special savings provisions.

1 "SEC. 30. ROTH IRAS.

2	"(a) General Rule.—Except as provided in this
3	section, a Roth IRA shall be treated for purposes of this
4	title in the same manner as an individual retirement plan.
5	"(b) ROTH IRA.—'Roth IRA' means an individual
6	retirement plan (as defined in section 7701(a)(37)) which
7	is designated (in such manner as the Secretary may pre-
8	scribe) at the time of establishment of the plan as a Roth
9	IRA. Such designation shall be made in such manner as
10	the Secretary may prescribe.
11	"(c) Treatment of Contributions.—
12	"(1) No deduction allowed.—No deduction
13	shall be allowed for a contribution to a Roth IRA.
14	"(2) Contribution Limit.—The aggregate
15	amount of contributions for any taxable year to all
16	Roth IRAs maintained for the benefit of an individ-
17	ual (or, in the case of individuals filing a joint re-
18	turn, either spouse) shall not exceed the taxpayer's
19	adjusted gross income for the taxable year.
20	"(3) Rollover from Ira.—
21	"(A) Rollover contributions.—No
22	rollover contribution may be made to a Roth
23	IRA unless it is a qualified rollover contribu-
24	tion.
25	"(B) LIMITS.—A taxpayer shall not be al-
26	lowed to make a qualified rollover contribution

1	to a Roth IRA from an individual retirement
2	plan other than a Roth IRA during any taxable
3	year if—
4	"(i) the taxpayer's adjusted gross in-
5	come for such taxable year exceeds
6	\$100,000, or
7	"(ii) the taxpayer is a married individ-
8	ual filing a separate return.
9	"(C) Marital Status.—Section 31(g)(4)
10	shall apply for purposes of this paragraph.
11	"(4) Contributions permitted after age
12	70½.—Contributions to a Roth IRA may be made
13	even after the individual for whom the account is
14	maintained has attained age $70^{1/2}$.
15	"(5) Mandatory distribution rules not
16	TO APPLY BEFORE DEATH.—Notwithstanding sub-
17	sections (a)(6) and (b)(3) of section 408 (relating to
18	required distributions), the following provisions shall
19	not apply to any Roth IRA:
20	"(A) Section 401(a)(9)(A).
21	"(B) The incidental death benefit require-
22	ments of section 401(a).
23	"(6) Time when contributions made.—A
24	taxpayer shall be deemed to have made a contribu-
25	tion to a Roth IRA during a year if the contribution

1	is made on account of such year and is made not
2	later than April 15 of the following year.
3	"(d) Exclusion From Income.—For purposes of
4	this chapter—
5	"(1) General rules.—A distribution from a
6	Roth IRA shall not be includible in gross income.
7	"(2) Nonqualified distribution.—The
8	automatic exclusion from gross income under para-
9	graph (1) shall not apply to any distribution, other
10	than a qualified special purpose distribution if—
11	"(A) it is made within the 5-taxable year
12	period beginning with the 1st taxable year for
13	which the individual made a contribution to a
14	Roth IRA (or such individual's spouse made a
15	contribution to a Roth IRA) established for
16	such individual, or
17	"(B) in the case of a payment or distribu-
18	tion properly allocable (as determined in the
19	manner prescribed by the Secretary) to a quali-
20	fied rollover contribution from an individual re-
21	tirement plan other than a Roth IRA (or in-
22	come allocable thereto), it is made within the 5-
23	taxable year period beginning with the taxable
24	year in which the rollover contribution was
25	made.

1 "(3) Nonqualified distributions.—In ap-2 plying section 33 to any distribution from a Roth 3 IRA described in paragraph (2), such distribution shall be treated as made from contributions to the 5 Roth IRA to the extent that such distribution, when 6 added to all previous distributions from the Roth 7 IRA, does not exceed the aggregate amount of con-8 tributions to the Roth IRA. Only distributions at-9 tributable to earnings on accounts (as opposed to 10 distributions of contributions) shall be included in 11 gross income.

"(4) ROLLOVERS FROM AN IRA OTHER THAN A ROTH IRA.—

"(A) IN GENERAL.—Notwithstanding section 408(d)(3), in the case of any distribution to which this paragraph applies there shall be included in gross income any amount which would be includible were it not part of a qualified rollover contribution.

"(B) DISTRIBUTIONS TO WHICH PARA-GRAPH APPLIES.—This paragraph shall apply to a distribution from an individual retirement plan (other than a Roth IRA) maintained for the benefit of an individual which is contributed to a Roth IRA maintained for the benefit of

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such individual in a qualified rollover contribution.

"(C) Conversions.—The conversion of an individual retirement plan (other than a Roth IRA) to a Roth IRA shall be treated for purposes of this paragraph as a distribution to which this paragraph applies.

"(D) Conversion of excess contributions.—If, no later than the due date for filing
the return of tax for any taxable year (without
regard to extensions), an individual transfers,
from an individual retirement plan (other than
a Roth IRA), contributions for such taxable
year (and any earnings allocable thereto) to a
Roth IRA, no such amount shall be includible
in gross income to the extent no deduction was
allowed with respect to such amount.

"(E) Additional Reporting Require-Ments.—Trustees of Roth IRAs, trustees of individual retirement plans, or both, whichever is appropriate, shall include such additional information in reports required under section 408(i) as the Secretary may require to ensure that amounts required to be included in gross income under subparagraph (A) are so included.

1	"(4) Coordination with individual retire-
2	MENT ACCOUNTS.—Section 408(d)(2) shall be ap-
3	plied separately with respect to Roth IRAs and other
4	individual retirement plans.
5	"(5) Qualified special purpose distribu-
6	TION.—'Qualified special purpose distribution'
7	means—
8	"(i) Distributions upon death.—
9	Distributions made to a beneficiary (or to
10	the estate of the individual) on or after the
11	death of the individual.
12	"(ii) Distributions upon disabil-
13	ITY.—Distributions attributable to the in-
14	dividual's being disabled.
15	"(iii) Distributions to pay medi-
16	CAL EXPENSES.—Distributions made to
17	the individual for amounts paid during the
18	year for medical care, but only to the ex-
19	tent that the amounts paid for medical
20	care exceed 7.5% of the adjusted gross in-
21	come of the taxpayer. (determined without
22	regard to whether the employee itemizes
23	deductions for such taxable year).
24	"(iv) QDROS.—Any distribution to
25	an alternate payee pursuant to a qualified

1	domestic relations order (within the mean-
2	ing of section $414(p)(1)$).
3	"(v) Distributions to unemployed
4	INDIVIDUALS FOR HEALTH INSURANCE
5	PREMIUMS.—Distributions to an
6	individual—
7	"(I) if such individual has re-
8	ceived unemployment compensation
9	for 12 consecutive weeks under any
10	Federal or State unemployment com-
11	pensation law by reason of such sepa-
12	ration (or in the case of a self-em-
13	ployed individual, to the extent pro-
14	vided in regulations, if the individual
15	would have received unemployment
16	compensation but for the fact the in-
17	dividual was self-employed),
18	"(II) if such distributions are
19	made during any taxable year during
20	which such unemployment compensa-
21	tion is paid or the succeeding taxable
22	year,
23	"(III) to the extent such distribu-
24	tions do not exceed the amount paid
25	during the taxable year for insurance

1 for the diagnosis, cure, mitigation, 2 treatment, or prevention of disease, or 3 for the purpose of affecting any structure or function of the body (or for transportation primarily for and es-6 sential to such medical care) (includ-7 ing amounts paid as premiums under 8 part B of title XVIII of the Social Se-9 curity Act, relating to supplementary 10 medical insurance for the aged) or for 11 any qualified long-term care insurance defined 12 contract in section (as 13 7702B(b)) with respect to the individ-14 ual and the individual's spouse and 15 dependents, and "(IV) such distributions are not 16 17 made after the individual has been 18 employed for at least 60 days after 19 the separation from employment to 20 which clause (I) applies. "(v) Distributions to pay higher 21 22 EDUCATION EXPENSES.—Distributions to 23 the extent such distributions do not exceed 24 the qualified higher education expenses (as 25 defined in section 10(a)(2) of—

1	"(I) the taxpayer,
2	"(II) the taxpayer's spouse, or
3	"(III) any child or grandchild of
4	the taxpayer or the taxpayer's spouse.
5	"(vi) Distributions for first
6	HOME PURCHASES.—Distributions which
7	are qualified first-time homebuyer distribu-
8	tions (as defined in paragraph (6)).
9	"(6) Qualified first-time homebuyer dis-
10	TRIBUTIONS.—
11	"(A) In General.—'Qualified first-time
12	homebuyer distribution' means any payment or
13	distribution received by an individual to the ex-
14	tent such payment or distribution is used by the
15	individual before the close of the 120th day
16	after the day on which such payment or dis-
17	tribution is received to pay qualified acquisition
18	costs with respect to a principal residence of a
19	first-time homebuyer who is such individual, the
20	spouse of such individual, or any child, grand-
21	child, or ancestor of such individual or the indi-
22	vidual's spouse.
23	"(B) Lifetime dollar limitation.—
24	The aggregate amount of payments or distribu-
25	tions received by an individual which may be

1	treated as qualified first-time homebuyer dis-
2	tributions for any taxable year shall not exceed
3	the excess (if any) of—
4	"(i) \$10,000, over
5	"(ii) the aggregate amounts treated as
6	qualified first-time homebuyer distributions
7	with respect to such individual for all prior
8	taxable years.
9	"(C) QUALIFIED ACQUISITION COSTS.—
10	'Qualified acquisition costs' means the costs of
11	acquiring, constructing, or reconstructing a res-
12	idence. Such term includes any usual or reason-
13	able settlement, financing, or other closing
14	costs.
15	"(D) First-time homebuyer; other
16	DEFINITIONS.—For purposes of this
17	paragraph—
18	"(i) First-time Homebuyer.—
19	'First-time homebuyer' means any individ-
20	ual if such individual (and if married, such
21	individual's spouse) had no present owner-
22	ship interest in a principal residence dur-
23	ing the 2-year period ending on the date of
24	acquisition of the principal residence to
25	which this paragraph applies, and

1	"(ii) Date of acquisition.—'Date
2	of acquisition' means the date—
3	"(I) on which a binding contract
4	to acquire the principal residence to
5	which subparagraph (A) applies is en-
6	tered into, or
7	"(II) on which construction or re-
8	construction of such a principal resi-
9	dence is commenced.
10	"(E) Special rule where delay in ac-
11	QUISITION.—The Secretary shall prescribe rules
12	under which a distribution will not be penalized
13	if made in anticipation of being a qualified
14	first-time homeowner distribution but construc-
15	tion delays or other unanticipated factors delay
16	the closing.
17	"(e) Qualified Rollover Contribution.—For
18	purposes of this section, the term qualified rollover con-
19	tribution means a rollover contribution to a Roth IRA
20	from another such account, or from an individual retire-
21	ment plan, but only if such rollover contribution meets the
22	requirements of section 408(d)(3). For purposes of section
23	408(d)(3)(B), there shall be disregarded any qualified roll-
24	over contribution from an individual retirement plan
25	(other than a Roth IRA) to a Roth IRA.

1	"(f) Permitted Investments.—
2	"(1) Investment permitted.—A Roth IRA
3	shall not cease to be an individual retirement ac-
4	count pursuant to section 408(e)(2) solely because
5	funds from such account are used to make a debt
6	or equity investment in a controlled business entity.
7	"(2) Loans to a controlled business en-
8	TITY.—
9	"(A) Excess return.—If funds in a
10	Roth IRA are loaned to a controlled business
11	entity, any return on such loans in excess of a
12	fair return shall be treated as gross income of
13	the beneficiary that is then deposited in the
14	Roth IRA.
15	"(B) Loan.—For purposes of this section,
16	an amount shall be treated as loaned to a con-
17	trolled business entity only if—
18	"(i) the amount is treated in the
19	books and records of the business entity as
20	a loan,
21	"(ii) the transaction is reflected in a
22	written note or other evidence of indebted-
23	ness, and
24	"(iii) the business entity is required to
25	pay interest at least once per year and at

1	the time such loan is made it is reasonable
2	to expect that such interest will be paid on
3	a timely basis.
4	"(C) Fair return.—For purposes of this
5	subsection, a 'fair return' with respect to a loan
6	is interest at a rate not in excess of 3 percent-
7	age points plus the minimum rate of interest
8	that would have to be charged with respect to
9	such loan to prevent it from being a below-mar-
10	ket loan for purposes of section 7872 (deter-
11	mined as if section 7872 applied to such loan).
12	"(3) Equity investment in a controlled
13	BUSINESS ENTITY.—If funds in a Roth IRA are con-
14	tributed to the capital of, applied to acquire stock or
15	other equity interest in, or otherwise transferred to,
16	a controlled business entity in a transaction that is
17	not considered a loan for purposes of this sub-
18	section, any return on such equity shall be treated
19	as gross income of the beneficiary that is then de-
20	posited in the Roth IRA. The preceding sentence
21	shall not apply to—
22	"(A) the proceeds of the sale of such eq-
23	uity interest to a third party, or
24	"(B) the proceeds received by the Roth
25	IRA as the result of a complete redemption of

- the beneficiary's interest in the business entity (including any interests held through a Roth IRA).
- "(4) Controlled Business entity.—'Con-5 trolled business entity' means any business entity in 6 which the beneficiary of the Roth IRA holds at least a 5 percent interest in the profits and losses (after 7 8 taking into account the investment through the Roth 9 IRA) and in which an investment would cause the 10 Roth IRA to cease to be an individual retirement ac-11 count by reason of section 408(e)(2) but for this 12 subsection.
 - "(5) APPLICATION OF SECTION 4975.—Section 4975 shall not apply to a loan or equity investment by a Roth IRA in a controlled business entity.
 - "(6) Tax and penalty avoidance.—The Secretary shall prescribe regulations that prohibit the provisions of this subsection to be used to circumvent the application of subsection (d)(2) (relating to taxable distributions). The regulations shall not prohibit bona fide investments in controlled business entities. The regulations shall address loans to and investments in a controlled business entity that are used to fund distributions or dividends from the

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1	business entity to the account beneficiary or a mem-
2	ber of the beneficiary's family.
3	"SEC. 31. DEDUCTIBLE IRAS.
4	"(a) Allowance of Deduction.—The 'qualified
5	IRA deduction' shall be an amount equal to the qualified
6	retirement contributions of the individual for the taxable
7	year, except as limited by subsection (b).
8	"(b) Maximum Amount of Deduction.—
9	"(1) In general.—The amount allowable as a
10	deduction under subsection (a) to any individual for
11	any taxable year shall not exceed the lesser of—
12	"(A) \$2,000, or
13	"(B) an amount equal to the compensation
14	includible in the individual's gross income for
15	such taxable year.
16	"(2) Special rule for employer contribu-
17	TIONS UNDER SIMPLIFIED EMPLOYEE PENSIONS.—
18	This section shall not apply with respect to an em-
19	ployer contribution to a simplified employee pension.
20	"(3) Grandfathered Plans.—Notwithstand-
21	ing paragraph (1), the amount allowable as a deduc-
22	tion under subsection (a) with respect to any con-
23	tributions on behalf of an employee to a plan de-
24	scribed in section 501(c)(18) of the Internal Reve-
25	nue Code of 1986 shall not exceed the lesser of—

1	"(A) \$7,000, or
2	"(B) an amount equal to 25 percent of the
3	compensation (as defined in section $415(c)(3)$)
4	includible in the individual's gross income for
5	such taxable year.
6	"(4) Special rule for simple retirement
7	ACCOUNTS.—This section shall not apply with re-
8	spect to any amount contributed to a simple retire-
9	ment account established under section 408(p).
10	"(c) Special rules for certain married indi-
11	VIDUALS.—
12	"(1) In general.—In the case of an individual
13	to whom this paragraph applies for the taxable year,
14	the limitation of paragraph (1) of subsection (b)
15	shall be equal to the lesser of—
16	"(A) the dollar amount in effect under
17	subsection $(b)(1)(A)$ for the taxable year, or
18	"(B) the sum of—
19	"(i) the compensation includible in
20	such individual's gross income for the tax-
21	able year, plus
22	"(ii) the compensation includible in
23	the gross income of such individual's
24	spouse for the taxable year reduced by—

1	"(I) the amount allowed as a de-
2	duction under subsection (a) to such
3	spouse for such taxable year, and
4	"(II) the amount of any contribu-
5	tion on behalf of such spouse to a
6	Roth IRA under section 30 for such
7	taxable year.
8	"(2) Individuals to whom paragraph (1)
9	APPLIES.—Paragraph (1) shall apply to any individ-
10	ual if—
11	"(A) such individual files a joint return for
12	the taxable year, and
13	"(B) the amount of compensation (if any)
14	includible in such individual's gross income for
15	the taxable year is less than the compensation
16	includible in the gross income of such individ-
17	ual's spouse for the taxable year.
18	"(d) Other limitations and restrictions.—
19	"(1) Beneficiary must be under age
20	70½.—No deduction shall be allowed under this sec-
21	tion with respect to any qualified retirement con-
22	tribution for the benefit of an individual if such indi-
23	vidual has attained age $70\frac{1}{2}$ before the close of such
24	individual's taxable year for which the contribution
25	was made.

- 1 "(2) RECONTRIBUTED AMOUNTS.—No deduc-2 tion shall be allowed under this section with respect 3 to a rollover contribution described in section 402(c), 4 403(a)(4), 403(b)(8), or 408(d)(3).
- "(3) Amounts contributed under endowners 6 Ment contract.—In the case of an endowment 7 contract described in section 408(b), no deduction 8 shall be allowed under this section for that portion 9 of the amounts paid under the contract for the tax-10 able year which is properly allocable, under regula-11 tions prescribed by the Secretary, to the cost of life 12 insurance.
- "(4) DENIAL OF DEDUCTION FOR AMOUNT
 CONTRIBUTED TO INHERITED ANNUITIES OR ACCOUNTS.—No deduction shall be allowed under this
 section with respect to any amount paid to an inherited individual retirement account or individual retirement annuity (within the meaning of section
 408(d)(3)(C)(ii)).
- 20 "(e) QUALIFIED RETIREMENT CONTRIBUTION.—For 21 purposes of this section, the term 'qualified retirement 22 contribution' means—
- 23 "(1) any amount paid in cash for the taxable 24 year by or on behalf of an individual to an individual 25 retirement plan for such individual's benefit, and

1 "(2) any amount contributed on behalf of any 2 individual to a plan described in section 501(c)(18) 3 of the Internal Revenue Code of 1986.

"(f) OTHER DEFINITIONS AND SPECIAL RULES.—

- "(1) Compensation.—For purposes of this section, the term 'compensation' includes earned income (as defined in section 401(c)(2)). The term 'compensation' does not include any amount received as a pension or annuity and does not include any amount received as deferred compensation. The term 'compensation' shall include any alimony, child support and separate maintenance payments includible in the individual's gross income with respect to a divorce or separation instrument. For purposes of this paragraph, section 401(c)(2) shall be applied as if the term trade or business for purposes of section 1402 included service described in subsection (c)(6).
- "(2) Married Individuals.—The maximum deduction under subsection (b) shall be computed separately for each individual, and this section shall be applied without regard to any community property laws.
- "(3) TIME WHEN CONTRIBUTIONS DEEMED MADE.—For purposes of this section, a taxpayer shall be deemed to have made a contribution to an

- individual retirement plan during a year if the contribution is made on account of such year and is made not later than April 15 of the following year.
 - "(4) Reports.—The Secretary shall prescribe regulations which prescribe the time and the manner in which reports to the Secretary and plan participants shall be made by the plan administrator of a qualified employer or government plan receiving qualified voluntary employee contributions.
 - "(5) EMPLOYER PAYMENTS.—For purposes of this title, any amount paid by an employer to an individual retirement plan shall be treated as payment of compensation to the employee (other than a self-employed individual who is an employee within the meaning of section 401(c)(1)) includible in his gross income in the taxable year for which the amount was contributed, whether or not a deduction for such payment is allowable under this section to the employee.
 - "(6) Excess contributions treated as contribution made during subsequent year for which there is an unused limitation.—
- 23 "(A) IN GENERAL.—If for the taxable year 24 the maximum amount allowable as a deduction 25 under this section for contributions to an indi-

1	vidual retirement plan exceeds the amount con-
2	tributed, then the taxpayer shall be treated as
3	having made an additional contribution for the
4	taxable year in an amount equal to the lesser
5	of—
6	"(i) the amount of such excess, or
7	"(ii) the amount of the excess con-
8	tributions for such taxable year (deter-
9	mined under section 4973(b)(2) without
10	regard to subparagraph (C) thereof).
11	"(B) Amount contributed.—For pur-
12	poses of this paragraph, the amount
13	contributed—
14	"(i) shall be determined without re-
15	gard to this paragraph, and
16	"(ii) shall not include any rollover
17	contribution.
18	"(C) Special rule where excess de-
19	DUCTION WAS ALLOWED FOR CLOSED YEAR.—
20	Proper reduction shall be made in the amount
21	allowable as a deduction by reason of this para-
22	graph for any amount allowed as a deduction
23	under this section for a prior taxable year for
24	which the period for assessing deficiency has ex-
25	pired if the amount so allowed exceeds the

1	amount which should have been allowed for
2	such prior taxable year.
3	"(7) Election not to deduct contribu-
4	TIONS.—For election not to deduct contributions to
5	individual retirement plans, see section
6	408(o)(2)(B)(ii).
7	"(g) Limitation on Deduction for Active Par-
8	TICIPANTS IN CERTAIN PENSION PLANS.—
9	"(1) In general.—If (for any part of any plan
10	year ending with or within a taxable year) an indi-
11	vidual is an active participant, each of the dollar
12	limitations contained in subsections $(b)(1)(A)$ and
13	(c)(1)(A) for such taxable year shall be reduced (but
14	not below zero) by the amount determined under
15	paragraph (2).
16	"(2) Amount of reduction.—
17	"(A) IN GENERAL.—The amount deter-
18	mined under this paragraph with respect to any
19	dollar limitation shall be the amount which
20	bears the same ratio to such limitation as—
21	"(i) the excess of—
22	"(I) the taxpayer's adjusted
23	gross income for such taxable year,
24	over

1	"(II) the applicable dollar
2	amount, bears to
3	"(ii) \$10,000 (\$20,000 in the case of
4	a joint return for a taxable year beginning
5	after December 31, 2006).
6	"(B) NO REDUCTION BELOW \$200 UNTIL
7	COMPLETE PHASE-OUT.—No dollar limitation
8	shall be reduced below \$200 under paragraph
9	(1) unless (without regard to this subpara-
10	graph) such limitation is reduced to zero.
11	"(C) ROUNDING.—Any amount determined
12	under this paragraph which is not a multiple of
13	\$10 shall be rounded to the next lowest \$10.
14	"(3) Adjusted gross income; applicable
15	DOLLAR AMOUNT.—For purposes of this
16	subsection—
17	"(A) Adjusted Gross Income.—Ad-
18	justed gross income of any taxpayer shall be de-
19	termined without regard to the qualified IRA
20	deduction.
21	"(B) APPLICABLE DOLLAR AMOUNT.—The
22	term 'applicable dollar amount' means the fol-
23	lowing:
24	"(i) In the case of a taxpayer filing a
25	joint return:

	"For taxable years beginning		dollar amount
	in: 1999	is: \$51,000	
	2000	\$52,000	
	2001	\$53,000	
	2002	\$54,000	
	2003	\$60,000	
	2004	\$65,000	
	2005	\$70,000	
	2006	+ ,	
	2007 and thereafter	\$80,000.	
1	"(ii) In	the case of any o	other taxpayer
2	(other than	a married indiv	idual filing a
3	separate retu	ırn):	
	For taxable years beginning in:	The applicable is:	dollar amount
	1999	\$31,000	
	2000	\$32,000	
	2001	\$33,000	
	2002	\$34,000	
	2003 2004	\$40,000 \$45,000	
	2005 and thereafter	,	
		,	
4	"(iii) In	the case of a m	arried individ-
5	ual filing a s	eparate return, z	ero.
6	"(4) Special Rul	LE FOR MARRIED	INDIVIDUALS
7	FILING SEPARATELY	AND LIVING AP.	ART.—A hus-
8	band and wife who—		
9	"(A) file sep	parate returns fo	or any taxable
10	year, and		
11	"(B) live ap	part at all times	during such
12	taxable year, shal	l not be treated	as married in-
13	dividuals for purp	ooses of this subs	ection.

1	"(5) ACTIVE PARTICIPANT.—For purposes of
2	this subsection, the term 'active participant' means,
3	with respect to any plan year, an individual—
4	"(A) who is an active participant in—
5	"(i) a plan described in section 401(a)
6	which includes a trust exempt from tax,
7	"(ii) an annuity plan described in sec-
8	tion 403(a),
9	"(iii) a plan established for its em-
10	ployees by the United States, by a State or
11	political subdivision thereof, or by an agen-
12	cy or instrumentality of any of the fore-
13	going,
14	"(iv) an annuity contract described in
15	section 403(b),
16	"(v) a simplified employee pension
17	(within the meaning of section 408(k)), or
18	"(vi) any simple retirement account
19	(within the meaning of section 408(p), or
20	"(B) who makes deductible contributions
21	to a trust described in section 501(c)(18).
22	The determination of whether an individual is an ac-
23	tive participant shall be made without regard to
24	whether or not such individual's rights under a plan,
25	trust, or contract are nonforfeitable. An eligible de-

1	ferred compensation plan (within the meaning of
2	section 457(b) of the Internal Revenue Code of
3	1986) shall not be treated as a plan described in
4	subparagraph (A)(iii).
5	"(6) Certain individuals not treated as
6	ACTIVE PARTICIPANTS.—For purposes of this sub-
7	section, any individual described in any of the follow-
8	ing subparagraphs shall not be treated as an active
9	participant for any taxable year solely because of
10	any participation so described:
11	"(A) Members of Reserve Compo-
12	NENTS.—Participation in a plan described in
13	subparagraph (A)(iii) of paragraph (5) by rea-
14	son of service as a member of a reserve compo-
15	nent of the Armed Forces (as defined in section
16	10101 of title 10, unless such individual has
17	served in excess of 90 days on active duty
18	(other than active duty for training) during the
19	year.
20	"(B) Volunteer firefighters.—A vol-
21	unteer firefighter—
22	"(i) who is a participant in a plan de-
23	scribed in subparagraph (A)(iii) of para-
24	graph (5) based on his activity as a volun-
25	teer firefighter, and

1	"(ii) whose accrued benefit as of the
2	beginning of the taxable year is not more
3	than an annual benefit of \$1,800 (when
4	expressed as a single life annuity com-
5	mencing at age 65).
6	"(7) Special rule for certain spouses.—
7	In the case of an individual who is an active partici-
8	pant at no time during any plan year ending with
9	or within the taxable year but whose spouse is an
10	active participant for any part of any such plan
11	year—
12	"(A) the applicable dollar amount under
13	paragraph (3)(B)(i) with respect to the tax-
14	payer shall be \$150,000, and
15	"(B) the amount applicable under para-
16	graph (2)(A)(ii) shall be \$10,000.
17	"(h) Cross Reference.—For failure to provide re-
18	quired reports, see section 6652(g).
19	"SEC. 32. EFFECT OF REPEAL OF SPECIAL SAVINGS PROVI-
20	SIONS.
21	"(a) Education IRA's.—
22	"(1) In general.—An account that qualifies
23	as an education IRA under the Internal Revenue
24	Code of 1986 as in effect immediately before adop-
25	tion of the Simplified USA Tax Act shall be treated

1	as a Roth IRA for purposes of this chapter (includ-
2	ing rules allowing for tax-free rollover).
3	"(2) No new contributions.—Neither para-
4	graph (1) nor section 530 of the Internal Revenue
5	Code of 1986 shall apply to an education IRA to
6	which contributions are made after December 31
7	1998.
8	"(3) Special rule.—For purposes of applying
9	section 30 to an account that was an educational
10	IRA, the designated beneficiary of such account
11	shall be treated as described in a subclause of clause
12	(vi) of section $30(d)(5)$.
13	"(b) Medical Savings Accounts.—
14	"(1) Equivalent of deductible ira.—A
15	medical savings account shall be treated as an indi-
16	vidual retirement plan other than a Roth IRA for
17	purposes of this chapter and chapter 3.
18	"(2) Special rollover rules.—
19	"(A) NO INCOME LIMIT.—The income lim-
20	its of section 30(c)(3)(B) shall not apply to the
21	rollover of a medical savings account into a
22	Roth IRA.
23	"(B) Medical distributions.—For pur-
24	poses of applying section 30 to the amount of
25	any medical savings account rolled over to a

1 Roth IRA, subclause (iii) of section 30(d)(5) 2 shall apply without regard to the limitation 3 based on adjusted gross income.

"(3) Medical savings account.—'Medical savings account' means an account established under section 220 of the Internal Revenue Code of 1986.
"(c) Qualified State Tuition Programs.—

"(1) Education savings account programs.—No account shall fail to qualify as a Roth IRA merely because in addition to the beneficiary of the account, there is a 'designated beneficiary' whose education expenses the beneficiary expects to pay or have paid with the proceeds of the account. The payment of such expenses with the proceeds of an account shall be treated as a distribution from the account.

"(2) Prepaid Tuition Certificates.—

"(A) Contribution to accounts.—An individual may contribute prepaid tuition certificates to a Roth IRA before January 1, 2002, without recognizing gross income on the contribution of such certificates. For purposes of section 30, the amount contributed shall equal the cost of the certificates.

1	"(B) Purchase of Prepaid Tuition
2	CERTIFICATES.—A Roth IRA account may pur-
3	chase prepaid tuition certificates without violat-
4	ing section 408.
5	"(C) Prepaid Tuition Certificates.—
6	'Prepaid tuition certificates' means credits or
7	certificates that entitle a designated beneficiary
8	of such certificates to the waiver or payment of
9	qualified higher education expenses of the des-
10	ignated beneficiary.
11	"(3) ROLLOVER OF ACCOUNTS.—An account to
12	which section 529 of the Internal Revenue Code of
13	1986 (before adoption of the Simplified USA Tax
14	Act) shall be treated as a Roth IRA for purposes of
15	rules relating to qualified rollovers (except that in
16	the case of any such rollover, any contributions
17	made to the section 529 account after July 1, 1998,
18	shall be treated as contributions to the Roth IRA in
19	the year of the rollover for purposes of section
20	30(e)(2)).
21	"(4) Transition.—
22	"(A) Transition Period.—Subsections
23	(a) and (c) of section 529 of the Internal Reve-
24	nue Code of 1986 shall apply until January 1,
25	2002.

1	"(B) Transition.—The Secretary shall
2	prescribe rules to facilitate use of the Roth IRA
3	rules to exempt earnings on accounts and cer-
4	tificates previously exempted under section 529
5	of the Internal Revenue Code of 1986.
6	"(5) Qualified higher education ex-
7	PENSES.—For purposes of this subsection, the defi-
8	nition 'qualified higher education expenses' in sec-
9	tion 529(e)(3) of the Internal Revenue Code of 1986
10	shall apply.
11	"SEC. 33. ANNUITIES, CERTAIN PROCEEDS OF ENDOWMENT
12	AND LIFE INSURANCE CONTRACTS.
13	"(a) General Rule for Annuities.—Except as
	• /
14	otherwise provided in this chapter, gross income includes
14 15	
15	otherwise provided in this chapter, gross income includes
15 16	otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period
15 16	otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, en-
15 16 17	otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, en- dowment, or life insurance contract.
15 16 17 18	otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, endowment, or life insurance contract. "(b) Exclusion Ratio.—
15 16 17 18 19	otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, endowment, or life insurance contract. "(b) Exclusion Ratio.— "(1) In general.—Gross income does not in-
15 16 17 18 19 20	otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, endowment, or life insurance contract. "(b) Exclusion Ratio.— "(1) In general.—Gross income does not include that part of any amount received as an annu-
15 16 17 18 19 20 21	otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, endowment, or life insurance contract. "(b) Exclusion Ratio.— "(1) In general.—Gross income does not include that part of any amount received as an annuity under an annuity, endowment, or life insurance

contract (as of such date).

1	"(2) Exclusion limited to investment.—
2	The portion of any amount received as an annuity
3	which is excluded from gross income under para-
4	graph (1) shall not exceed the unrecovered invest-
5	ment in the contract immediately before the receipt
6	of such amount.
7	"(3) Deduction where annuity payments
8	CEASE BEFORE ENTIRE INVESTMENT RECOVERED.—
9	"(A) In general.—If—
10	"(i) after the annuity starting date,
11	payments as an annuity under the contract
12	cease by reason of the death of an annu-
13	itant, and
14	"(ii) as of the date of such cessation,
15	there is unrecovered investment in the con-
16	tract,
17	the amount of such unrecovered investment (in
18	excess of any amount specified in subsection
19	(e)(5) which was not included in gross income)
20	shall be allowed as a deduction from adjusted
21	gross income in determining taxable income of
22	the annuitant for his last taxable year.
23	"(B) Payments to other persons.—In
24	the case of any contract which provides for pay-
25	ments meeting the requirements of subpara-

1 graphs (B) and (C) of subsection (c)(2), the de-2 duction under subparagraph (A) shall be al-3 lowed to the person entitled to such payments 4 for the taxable year in which such payments are received. 6 "(c) Definitions.— 7 "(1) INVESTMENT IN THE CONTRACT.—For 8 purposes of subsection (b), the investment in the 9 contract as of the annuity starting date is— "(A) the aggregate amount of premiums or 10 11 other consideration paid for the contract (in-12 cluding any amounts earned on the contract 13 which were included in gross income and rein-14 vested in the contract), minus "(B) the aggregate amount received under 15 16 the contract before such date, to the extent that 17 such amount was excludable from gross income 18 under this subtitle or prior income tax laws. 19 "(2) OTHER TERMS USED IN SUBSECTION (b).—Calculations under subsections (a) and (b) 20 21 shall be made in accordance with regulations pre-

scribed by the Secretary, which regulations shall

generally be consistent with the section 72 of the In-

ternal Revenue Code of 1986.

22

23

1	"(d) Special Rules for Qualified Employer
2	RETIREMENT PLANS.—
3	"(1) Simplified method of taxing annuity
4	PAYMENTS.—
5	"(A) In General.—In the case of any
6	amount received as an annuity under a quali-
7	fied employer retirement plan—
8	"(i) subsection (b) shall not apply,
9	and
10	"(ii) the investment in the contract
11	shall be recovered as provided in this para-
12	graph.
13	"(B) Method of recovering invest-
14	MENT IN CONTRACT.—
15	"(i) In general.—Gross income
16	shall not include so much of any monthly
17	annuity payment under a qualified em-
18	ployer retirement plan as does not exceed
19	the amount obtained by dividing—
20	"(I) the investment in the con-
21	tract (as of the annuity starting date),
22	by
23	"(II) the number of anticipated
24	payments determined under the table
25	contained in clause (iii) (or, in the

1	case of a contract to which subsection
2	(c)(3)(B) applies, the number of
3	monthly annuity payments under such
4	contract).
5	"(ii) Certain rules made applica-
6	BLE.—Rules similar to the rules of para-
7	graphs (2) and (3) of subsection (b) shall
8	apply for purposes of this paragraph.
9	"(iii) Number of anticipated pay-
10	MENTS.—If the annuity is payable over the
11	life of a single individual, the number of
12	anticipated payments shall be determined
13	as follows:

If the age of the annuitant on the number: the annuity starting date

is:	
Not more than 55	360
More than 55 but not more than	310
60.	
More than 60 but not more than	260
65.	
More than 65 but not more than	210
70.	
More than 70	160

"(iv) Number of anticipated pay15 Ments where more than one life.—If
16 the annuity is payable over the lives of
17 more than 1 individual, the number of an18 ticipated payments shall be determined as
19 follows:

If the combined ages of the The number: annuitants are: Not more than 110 410 More than 110 but not more than 360 120. More than 120 but not more than 310 130. More than 130 but not more than 260 More than 140 210 1 "(C) Special rule where lump sum 2 PAID IN CONNECTION WITH COMMENCEMENT 3 OF ANNUITY PAYMENTS.—If, in connection with 4 the commencement of annuity payments under 5 any qualified employer retirement plan, the tax-6 payer receives a lump sum payment— "(i) such payment shall be taxable 7 under subsection (e) as if received before 8 9 the annuity starting date, and 10 "(ii) the investment in the contract 11 for purposes of this paragraph shall be de-12 termined as if such payment had been so 13 received. 14 "(D) Exception.—This paragraph shall 15 not apply in any case where the primary annu-16 itant has attained age 75 on the annuity start-17 ing date unless there are fewer than 5 years of 18 guaranteed payments under the annuity. 19 "(E) Adjustment where annuity pay-20 MENTS NOT ON A MONTHLY BASIS.—In any

1	case where the annuity payments are not made
2	on a monthly basis, appropriate adjustments in
3	the application of this paragraph shall be made
4	to take into account the period on the basis of
5	which such payments are made.
6	"(F) QUALIFIED EMPLOYER RETIREMENT
7	PLAN.—For purposes of this paragraph, the
8	term 'qualified employer retirement plan' means
9	any plan or contract described in paragraph
10	(1), (2), or (3) of section 4974(c).
11	"(2) Treatment of employee contribu-
12	TIONS UNDER DEFINED CONTRIBUTION PLANS.—
13	For purposes of this section, employee contributions
14	(and any income allocable thereto) under a defined
15	contribution plan may be treated as a separate con-
16	tract.
17	"(e) Amounts Not Received as Annuities.—
18	"(1) Application of subsection.—
19	"(A) In general.—This subsection shall
20	apply to any amount which—
21	"(i) is received under an annuity, en-
22	dowment, or life insurance contract, and
23	"(ii) is not received as an annuity,

1	if no provision of this subtitle (other than this
2	subsection) applies with respect to such
3	amount.
4	"(B) DIVIDENDS.—For purposes of this
5	section, any amount received which is in the na-
6	ture of a dividend or similar distribution shall
7	be treated as an amount not received as an an-
8	nuity.
9	"(2) General Rule.—Any amount to which
10	this subsection applies—
11	"(A) if received on or after the annuity
12	starting date, shall be included in gross income,
13	or
14	"(B) if received before the annuity starting
15	date—
16	"(i) shall be included in gross income
17	to the extent allocable to income on the
18	contract, and
19	"(ii) shall not be included in gross in-
20	come to the extent allocable to the invest-
21	ment in the contract.
22	"(3) Allocation of amounts to income
23	AND INVESTMENT.—For purposes of paragraph
24	(2)(B):

1	"(A) Any amount to which this subsection
2	applies shall be treated as allocable to income
3	on the contract to the extent that such amount
4	does not exceed the excess (if any) of—
5	"(i) the cash value of the contract
6	(determined without regard to any surren-
7	der charge) immediately before the amount
8	is received, over
9	"(ii) the investment in the contract at
10	such time.
11	"(B) Any amount to which this subsection
12	applies shall be treated as allocable to invest-
13	ment in the contract to the extent that such
14	amount is not allocated to income under sub-
15	paragraph (A).
16	"(4) Special rules for application of
17	PARAGRAPH (2)(B).—For purposes of paragraph
18	(2)(B):
19	"(A) Loans treated as distribu-
20	TIONS.—If, during any taxable year, an
21	individual—
22	"(i) receives (directly or indirectly)
23	any amount as a loan under any contract
24	to which this subsection applies, or

1	"(ii) assigns or pledges (or agrees to
2	assign or pledge) any portion of the value
3	of any such contract,
4	such amount or portion shall be treated as re-
5	ceived under the contract as an amount not re-
6	ceived as an annuity. The preceding sentence
7	shall not apply for purposes of determining in-
8	vestment in the contract, except that the invest-
9	ment in the contract shall be increased by any
10	amount included in gross income by reason of
11	the amount treated as received under the pre-
12	ceding sentence.
13	"(B) Treatment of transfers with-
14	OUT ADEQUATE CONSIDERATION.—
15	"(i) In general.—If an individual
16	who holds an annuity contract transfers it
17	without full and adequate consideration,
18	such individual shall be treated as receiv-
19	ing an amount equal to the excess of—
20	"(I) the cash surrender value of
21	such contract at the time of transfer,
22	over
23	"(II) the investment in such con-
24	tract at such time,

1	under the contract as an amount not re-
2	ceived as an annuity.
3	"(ii) Exception for certain
4	TRANSFERS BETWEEN SPOUSES OF
5	FORMER SPOUSES.—Clause (i) shall not
6	apply to any transfer to which section
7	77(c) (relating to transfers of property be-
8	tween spouses or incident to divorce) ap-
9	plies.
10	"(iii) Adjustment to investment
11	IN CONTRACT OF TRANSFEREE.—If under
12	clause (i) an amount is included in the
13	gross income of the transferor of an annu-
14	ity contract, the investment in the contract
15	of the transferee in such contract shall be
16	increased by the amount so included.
17	"(5) Retention of existing rules in cer-
18	TAIN CASES.—Paragraph (5) of section 72(e) of the
19	Internal Revenue Code of 1986 shall apply to con-
20	tracts described in subparagraph (B) of such para-
21	graph to the extent provided therein.
22	"(6) Investment in the contract.—For
23	purposes of this subsection, the investment in the
24	contract as of any date is—

1	"(A) the aggregate amount of premiums or
2	other consideration paid for the contract before
3	such date, minus
4	"(B) the aggregate amount received under
5	the contract before such date, to the extent that
6	such amount was excludable from gross income
7	under this subtitle or prior income tax laws.
8	"(7) Application of Paragraph (2)(B) to
9	QUALIFIED PLANS.—
10	"(A) In General.—Notwithstanding any
11	other provision of this subsection, in the case of
12	any amount received before the annuity starting
13	date from a trust or contract described in para-
14	graph (5)(D), paragraph (2)(B) shall apply to
15	such amounts.
16	"(B) Allocation of amount re-
17	CEIVED.—For purposes of paragraph (2)(B),
18	the amount allocated to the investment in the
19	contract shall be the portion of the amount de-
20	scribed in subparagraph (A) which bears the
21	same ratio to such amount as the investment in
22	the contract bears to the account balance. The
23	determination under the preceding sentence
24	shall be made as of the time of the distribution

1	or at such other time as the Secretary may pre-
2	scribe.
3	"(C) Treatment of forfeitable
4	RIGHTS.—If an employee does not have a non-
5	forfeitable right to any amount under any trust
6	or contract to which subparagraph (A) applies
7	such amount shall not be treated as part of the
8	account balance.
9	"(D) Investment in the contract be-
10	FORE 1987.—In the case of a plan which on
11	May 5, 1986, permitted withdrawal of any em-
12	ployee contributions before separation from
13	service, subparagraph (A) shall apply only to
14	the extent that amounts received before the an-
15	nuity starting date (when increased by amounts
16	previously received under the contract after De-
17	cember 31, 1986) exceed the investment in the
18	contract as of December 31, 1986.
19	"(8) Treatment of modified endowment
20	CONTRACTS.—
21	"(A) In general.—Notwithstanding para-
22	graph (5)(C), in the case of any modified en-
23	dowment contract (as defined in section
24	7702A)—

1	"(i) paragraphs $(2)(B)$ and $(4)(A)$
2	shall apply, and
3	"(ii) in applying paragraph (4)(A),
4	'any person' shall be substituted for 'an in-
5	dividual'.
6	"(B) Treatment of certain burial
7	CONTRACTS.—Notwithstanding subparagraph
8	(A), paragraph (4)(A) shall not apply to any as-
9	signment (or pledge) of a modified endowment
10	contract if such assignment (or pledge) is solely
11	to cover the payment of expenses referred to in
12	section 7702(e)(2)(C)(iii) and if the maximum
13	death benefit under such contract does not ex-
14	ceed \$25,000.
15	"(9) Anti-abuse rules.—
16	"(A) In general.—For purposes of deter-
17	mining the amount includible in gross income
18	under this subsection—
19	"(i) all modified endowment contracts
20	issued by the same company to the same
21	policyholder during any calendar year shall
22	be treated as 1 modified endowment con-
23	tract, and
24	"(ii) all annuity contracts issued by
25	the same company to the same policyholder

1	during any calendar year shall be treated
2	as 1 annuity contract.
3	The preceding sentence shall not apply to any
4	contract described in paragraph (5)(D).
5	"(B) REGULATORY AUTHORITY.—The Sec-
6	retary may by regulations prescribe such addi-
7	tional rules as may be necessary or appropriate
8	to prevent avoidance of the purposes of this
9	subsection through serial purchases of contracts
10	or otherwise.
11	"(f) Special Rules for Computing Employees"
12	CONTRIBUTIONS.—In computing, for purposes of sub-
13	section (c)(1)(A), the aggregate amount of premiums or
14	other consideration paid for the contract, and for purposes
15	of subsection (e)(6), the aggregate premiums or other con-
16	sideration paid, amounts contributed by the employer shall
17	be included, but only to the extent that—
18	"(1) such amounts were includible in the gross
19	income of the employee under this subtitle or prior
20	income tax laws; or
21	"(2) if such amounts had been paid directly to
22	the employee at the time they were contributed, they
23	would not have been includible in the gross income
24	of the employee under the law applicable at the time
25	of such contribution.

1	"(g) Rules for Transferee Where Transfer
2	Was for Value.—Where any contract (or any interest
3	therein) is transferred (by assignment or otherwise) for
4	a valuable consideration, to the extent that the contract
5	(or interest therein) does not, in the hands of the trans-
6	feree, have a basis which is determined by reference to
7	the basis in the hands of the transferor, then—
8	"(1) for purposes of this section, only the ac-
9	tual value of such consideration, plus the amount of
10	the premiums and other consideration paid by the
11	transferee after the transfer, shall be taken into ac-
12	count in computing the aggregate amount of the
13	premiums or other consideration paid for the con-
14	tract;
15	"(2) for purposes of subsection (c)(1)(B), there
16	shall be taken into account only the aggregate
17	amount received under the contract by the trans-
18	feree before the annuity starting date, to the extent
19	that such amount was excludable from gross income
20	under this subtitle or prior income tax laws; and
21	"(3) the annuity starting date is January 1,
22	1954, or the first day of the first period for which
23	the transferee received an amount under the con-
24	tract as an annuity, whichever is the later.

- 1 "(h) Option To Receive Annuity in Lieu of
- 2 Lump Sum.—If—
- 3 "(1) a contract provides for payment of a lump
- 4 sum in full discharge of an obligation under the con-
- 5 tract, subject to an option to receive an annuity in
- 6 lieu of such lump sum;
- 7 "(2) the option is exercised within 60 days after
- 8 the day on which such lump sum first became pay-
- 9 able; and
- 10 "(3) part or all of such lump sum would (but
- 11 for this subsection) be includible in gross income by
- reason of subsection (e)(1),
- 13 then, for purposes of this subtitle, no part of such lump
- 14 sum shall be considered as includible in gross income at
- 15 the time such lump sum first became payable.
- 16 "(i) Interest.—Notwithstanding any other provi-
- 17 sion of this section, if any amount is held under an agree-
- 18 ment to pay interest thereon, the interest payments shall
- 19 be included in gross income.
- 20 "(j) Face-Amount Certificates.—For purposes of
- 21 this section, the term 'endowment contract' includes a
- 22 face-amount certificate, as defined in section 2(a)(15) of
- 23 the Investment Company Act of 1940 (15 U.S.C., sec.
- 24 80a-2), issued after December 31, 1954.

1	"(k) Special Rules Applicable to Employee
2	Annuities and Distributions Under Employee
3	Plans.—
4	"(1) Computation of consideration paid
5	BY THE EMPLOYEE.—In computing—
6	"(A) the aggregate amount of premiums or
7	other consideration paid for the contract for
8	purposes of subsection (c)(1)(A) (relating to the
9	investment in the contract), and
10	"(B) the aggregate premiums or other con-
11	sideration paid for purposes of subsection (e)(6)
12	(relating to certain amounts not received as an
13	annuity),
14	any amount allowed as a deduction with respect to
15	the contract under section 404 which was paid while
16	the employee was an employee within the meaning of
17	section $401(c)(1)$ shall be treated as consideration
18	contributed by the employer, and there shall not be
19	taken into account any portion of the premiums or
20	other consideration for the contract paid while the
21	employee was an owner-employee which is properly
22	allocable (as determined under regulations pre-
23	scribed by the Secretary) to the cost of life, accident,
24	health, or other insurance.
25	"(2) Life insurance contracts.—

1	"(A) This paragraph shall apply to any life
2	insurance contract—
3	"(i) purchased as a part of a plan de-
4	scribed in section 403(a), or
5	"(ii) purchased by a trust described in
6	section 401(a) which is exempt from tax if
7	the proceeds of such contract are payable
8	directly or indirectly to a participant in
9	such trust or to a beneficiary of such par-
10	ticipant.
11	"(B) Any contribution to a plan described
12	in subparagraph (A)(i) or a trust described in
13	subparagraph (A)(ii) which is allowed as a de-
14	duction under section 404, and any income of
15	a trust described in subparagraph (A)(ii), which
16	is determined in accordance with regulations
17	prescribed by the Secretary to have been ap-
18	plied to purchase the life insurance protection
19	under a contract described in subparagraph
20	(A), is includible in the gross income of the par-
21	ticipant for the taxable year when so applied.
22	"(C) In the case of the death of an individ-
23	ual insured under a contract described in sub-
24	paragraph (A), an amount equal to the cash
25	surrender value of the contract immediately be-

fore the death of the insured shall be treated as a payment under such plan or a distribution by such trust, and the excess of the amount payable by reason of the death of the insured over such cash surrender value shall not be includible in gross income under this section and shall be treated as provided in section 101.

"(3) Penalties applicable to certain amounts received by 5-percent owners.—

"(A) This paragraph applies to amounts which are received from a qualified trust described in section 401(a) or under a plan described in section 403(a) at any time by an individual who is, or has been, a 5-percent owner, or by a successor of such an individual, but only to the extent such amounts are determined, under regulations prescribed by the Secretary, to exceed the benefits provided for such individual under the plan formula.

"(B) If a person receives an amount to which this paragraph applies, his tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the portion of

the amount so received which is includible in his gross income for such taxable year.

- "(C) For purposes of this paragraph, the term '5-percent owner' means any individual who, at any time during the 5 plan years preceding the plan year ending in the taxable year in which the amount is received, is a 5-percent owner (as defined in section 416(i)(1)(B).
- "(4) Owner-employee Defined.—For purposes of this subsection, the term 'owner-employee' has the meaning assigned to it by section 401(c)(3) and includes an individual for whose benefit an individual retirement account or annuity described in section 408(a) or (b) is maintained. For purposes of the preceding sentence, the term 'owner-employee' shall include an employee within the meaning of section 401(c)(1).
- "(5) Meaning of disabled.—For purposes of this section, an individual shall be considered to be disabled if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration. An individual shall not be considered to be disabled unless he furnishes proof

of the existence thereof in such form and manner as the Secretary may require.

"(6) DETERMINATION OF INVESTMENT IN THE CONTRACT IN THE CASE OF QUALIFIED DOMESTIC RELATIONS ORDERS.—Under regulations prescribed by the Secretary, in the case of a distribution or payment made to an alternate payee who is the spouse or former spouse of the participant pursuant to a qualified domestic relations order (as defined in section 414(p)), the investment in the contract as of the date prescribed in such regulations shall be allocated on a pro rata basis between the present value of such distribution or payment and the present value of all other benefits payable with respect to the participant to which such order relates.

"(I) Annuities Under Retired Serviceman's
17 Family Protection Plan or Survivor Benefit
18 Plan.—Subsection (b) shall not apply in the case of
19 amounts received after December 31, 1965, as an annuity
20 under chapter 73 of title 10 of the United States Code,
21 but all such amounts shall be excluded from gross income
22 until there has been so excluded (under section 122(b)(1)
23 of the Internal Revenue Code of 1986, section 93, or this
24 section, including amounts excluded before January 1,

1966) an amount equal to the consideration for the con-

1	tract (as defined by section 122(b)(2) of the Internal Rev-
2	enue Code of 1986). Thereafter all amounts so received
3	shall be included in gross income.
4	"(m) Special Rules for Distributions From
5	QUALIFIED PLANS TO WHICH EMPLOYEE MADE DE-
6	DUCTIBLE CONTRIBUTIONS.—
7	"(1) Treatment of contributions.—For
8	purposes of this section and sections 402 and 403,
9	notwithstanding section 414(h), any deductible em-
10	ployee contribution made to a qualified employer
11	plan or government plan shall be treated as an
12	amount contributed by the employer which is not in-
13	cludible in the gross income of the employee.
14	"(2) Amounts constructively received.—
15	"(A) IN GENERAL.—For purposes of this
16	subsection, rules similar to the rules provided
17	by subsection (n) (other than the exception con-
18	tained in paragraph (2) thereof) shall apply.
19	"(B) Purchase of Life Insurance.—To
20	the extent any amount of accumulated deduct-
21	ible employee contributions of an employee are
22	applied to the purchase of life insurance con-
23	tracts, such amount shall be treated as distrib-

uted to the employee in the year so applied.

1	"(3) Special rule for treatment of roll-
2	OVER AMOUNTS.—For purposes of sections 402(c),
3	403(a)(4), and $408(d)(3)$, the Secretary shall pre-
4	scribe regulations providing for such allocations of
5	amounts attributable to accumulated deductible em-
6	ployee contributions, and for such other rules, as
7	may be necessary to insure that such accumulated
8	deductible employee contributions do not become eli-
9	gible for additional tax benefits (or freed from limi-
10	tations) through the use of rollovers.
11	"(4) Ordering rules.—Unless the plan speci-
12	fies otherwise, any distribution from such plan shall
13	not be treated as being made from the accumulated
14	deductible employee contributions, until all other
15	amounts to the credit of the employee have been dis-
16	tributed.
17	"(n) Loans Treated as Distributions.—For pur-
18	poses of this section—
19	"(1) Treatment as distributions.—
20	"(A) Loans.—If during any taxable year a
21	participant or beneficiary receives (directly or
22	indirectly) any amount as a loan from a quali-
23	fied employer plan, such amount shall be treat-
24	ed as having been received by such individual as
25	a distribution under such plan.

1	"(B) Assignments or pledges.—If dur-
2	ing any taxable year a participant or beneficiary
3	assigns (or agrees to assign) or pledges (or
4	agrees to pledge) any portion of his interest in
5	a qualified employer plan, such portion shall be
6	treated as having been received by such individ-
7	ual as a loan from such plan.
8	"(2) Exception for certain loans.—
9	"(A) GENERAL RULE.—Paragraph (1)
10	shall not apply to any loan to the extent that
11	such loan (when added to the outstanding bal-
12	ance of all other loans from such plan whether
13	made on, before, or after August 13, 1982),
14	does not exceed the lesser of—
15	"(i) \$50,000, reduced by the excess (if
16	any) of—
17	"(I) the highest outstanding bal-
18	ance of loans from the plan during the
19	1-year period ending on the day be-
20	fore the date on which such loan was
21	made, over
22	"(II) the outstanding balance of
23	loans from the plan on the date on
24	which such loan was made, or

1	"(ii) the greater of (I) one-half of the
2	present value of the nonforfeitable accrued
3	benefit of the employee under the plan, or
4	(II) $$10,000$.
5	for purposes of clause (ii), the present value of
6	the nonforfeitable accrued benefit shall be de-
7	termined without regard to any accumulated
8	deductible employee contributions (as defined in
9	subsection $(m)(5)(B)$).
10	"(B) Requirement that loan be re-
11	PAYABLE WITHIN 5 YEARS.—
12	"(i) In General.—Subparagraph (A)
13	shall not apply to any loan unless such
14	loan, by its terms, is required to be repaid
15	within 5 years.
16	"(ii) Exception for home loans.—
17	Clause (i) shall not apply to any loan used
18	to acquire any dwelling unit which within
19	a reasonable time is to be used (deter-
20	mined at the time the loan is made) as the
21	principal residence of the participant.
22	"(C) Requirement of Level Amortiza-
23	TION.—Except as provided in regulations, this
24	paragraph shall not apply to any loan unless
25	substantially level amortization of such loan

1	(with payments not less frequently than quar-
2	terly) is required over the term of the loan.
3	"(D) Related employers and related
4	PLANS.—For purposes of this paragraph—
5	"(i) the rules of subsections (b), (c),
6	and (m) of section 414 shall apply, and
7	"(ii) all plans of an employer (deter-
8	mined after the application of such sub-
9	sections) shall be treated as 1 plan.
10	"(o) 10-Percent Penalty for Premature Dis-
11	TRIBUTIONS FROM ANNUITY CONTRACTS.—
12	"(1) Imposition of Penalty.—If any tax-
13	payer receives any amount under an annuity con-
14	tract, the taxpayer's tax under this chapter for the
15	taxable year in which such amount is received shall
16	be increased by an amount equal to 10 percent of
17	the portion of such amount which is includible in
18	gross income.
19	"(2) Subsection not to apply to certain
20	DISTRIBUTIONS.—Paragraph (1) shall not apply to
21	any distribution—
22	"(A) made on or after the date on which
23	the taxpayer attains age 59½,

1	"(B) made on or after the death of the
2	holder (or, where the holder is not an individ-
3	ual, the death of the primary annuitant),
4	"(C) attributable to the taxpayer's becom-
5	ing disabled within the meaning of subsection
6	(k)(5),
7	"(D) which is a part of a series of substan-
8	tially equal periodic payments (not less fre-
9	quently than annually) made for the life (or life
10	expectancy) of the taxpayer or the joint lives
11	(or joint life expectancies) of such taxpayer and
12	his designated beneficiary,
13	"(E) from a plan, contract, account, trust,
14	or annuity described in section $72(e)(5)(D)$ of
15	the Internal Revenue Code of 1986,
16	"(F) allocable to investment in the con-
17	tract before August 14, 1982,
18	"(G) under a qualified funding asset,
19	"(H) to which subsection (r) applies (with-
20	out regard to paragraph (2) thereof),
21	"(I) under an immediate annuity contract,
22	or
23	"(J) which is purchased by an employer
24	upon the termination of a plan described in sec-
25	tion 401(a) or 403(a) and which is held by the

1	employer until such time as the employee sepa-
2	rates from service.
3	"(3) Change in substantially equal pay-
4	MENTS.—If—
5	"(A) paragraph (1) does not apply to a
6	distribution by reason of paragraph (2)(D), and
7	"(B) the series of payments under such
8	paragraph are subsequently modified (other
9	than by reason of death or disability)—
10	"(i) before the close of the 5-year pe-
11	riod beginning on the date of the first pay-
12	ment and after the taxpayer attains age
13	$59\frac{1}{2}$, or
14	"(ii) before the taxpayer attains age
15	$59\frac{1}{2}$,
16	the taxpayer's tax for the 1st taxable year in which
17	such modification occurs shall be increased by an
18	amount, determined under regulations, equal to the
19	tax which (but for paragraph $(2)(D)$) would have
20	been imposed, plus interest for the deferral period
21	(within the meaning of subsection $(r)(4)(B)$).
22	"(p) Certain Railroad Retirement Benefits
23	TREATED AS RECEIVED UNDER EMPLOYER PLANS.—
24	"(1) In general.—Notwithstanding any other
25	provision of law, any benefit provided under the

1	Railroad Retirement Act of 1974 (other than a tier
2	1 railroad retirement benefit) shall be treated for
3	purposes of this title as a benefit provided under an
4	employer plan which meets the requirements of sec-
5	tion 401(a).
6	"(2) Tier 2 taxes treated as contribu-
7	TIONS.—For purposes of paragraph (1)—
8	"(i) the tier 2 portion of the tax im-
9	posed by section 3201 (relating to tax on
10	employees) shall be treated as an employee
11	contribution,
12	"(ii) the tier 2 portion of the tax im-
13	posed by section 3211 (relating to tax on
14	employee representatives) shall be treated
15	as an employee contribution, and
16	"(iii) the tier 2 portion of the tax im-
17	posed by section 3221 (relating to tax on
18	employers) shall be treated as an employer
19	contribution.
20	"(B) Tier 2 Portion.—For purposes of
21	subparagraph (A)—
22	"(1) After 1984.—With respect to compensa-
23	tion paid after 1984, the tier 2 portion shall be the
24	taxes imposed by sections 3201(b), 3211(a)(2), and
25	3221(b).

1	"(2) Before 1985.—With respect to compensa-
2	tion paid before 1985, see section 72(r) of Internal
3	Revenue Code of 1986 for the definition of tier 2
4	portion.
5	"(C) CONTRIBUTIONS NOT ALLOCABLE TO
6	SUPPLEMENTAL ANNUITY OR WINDFALL BENE-
7	FITS.—For purposes of paragraph (1), no
8	amount treated as an employee contribution
9	under this paragraph shall be allocated to—
10	"(i) any supplemental annuity paid
11	under section 2(b) of the Railroad Retire-
12	ment Act of 1974, or
13	"(ii) any benefit paid under section
14	3(h), 4(e), or 4(h) of such Act.
15	"(3) Tier 1 railroad retirement bene-
16	FIT.—For purposes of paragraph (1), the term 'tier
17	1 railroad retirement benefit' has the meaning given
18	such term by section 3(b)(2)(B).
19	"(q) Required Distributions Where Holder
20	DIES BEFORE ENTIRE INTEREST IS DISTRIBUTED.—
21	"(1) In general.—A contract shall not be
22	treated as an annuity contract for purposes of this
23	chapter unless it provides that—
24	"(A) if any holder of such contract dies on
25	or after the annuity starting date and before

1	the entire interest in such contract has been
2	distributed, the remaining portion of such inter-
3	est will be distributed at least as rapidly as
4	under the method of distributions being used as
5	of the date of his death, and
6	"(B) if any holder of such contract dies be-
7	fore the annuity starting date, the entire inter-
8	est in such contract will be distributed within 5
9	years after the death of such holder.
10	"(2) Exception for certain amounts pay-
11	ABLE OVER LIFE OF BENEFICIARY.—IF—
12	"(A) any portion of the holder's interest is
13	payable to (or for the benefit of) a designated
14	beneficiary,
15	"(B) such portion will be distributed (in
16	accordance with regulations) over the life of
17	such designated beneficiary (or over a period
18	not extending beyond the life expectancy of
19	such beneficiary), and
20	"(C) such distributions begin not later
21	than 1 year after the date of the holder's death
22	or such later date as the Secretary may by reg-
23	ulations prescribe,
24	then for purposes of paragraph (1), the portion re-
25	ferred to in subparagraph (A) shall be treated as

1	distributed on the day on which such distributions
2	begin.
3	"(3) Special rule where surviving spouse
4	BENEFICIARY.—If the designated beneficiary re-
5	ferred to in paragraph (2)(A) is the surviving spouse
6	of the holder of the contract, paragraphs (1) and (2)
7	shall be applied by treating such spouse as the hold-
8	er of such contract.
9	"(4) Designated Beneficiary.—For pur-
10	poses of this subsection, the term 'designated bene-
11	ficiary' means any individual designated a bene-
12	ficiary by the holder of the contract.
13	"(5) Exception for certain annuity con-
14	TRACTS.—This subsection shall not apply to any an-
15	nuity contract—
16	"(A) which is provided—
17	"(i) under a plan described in section
18	401(a) which includes a trust exempt from
19	tax under section 501, or
20	"(ii) under a plan described in section
21	403(a),
22	"(B) which is described in section 403(b),
23	"(C) which is an individual retirement an-
24	nuity or provided under an individual retire-
25	ment account or annuity, or

1	"(D) which is a qualified funding asset.
2	"(6) Special rule where holder is cor-
3	PORATION OR OTHER NON-INDIVIDUAL.—
4	"(A) In general.—For purposes of this
5	subsection, if the holder of the contract is not
6	an individual, the primary annuitant shall be
7	treated as the holder of the contract.
8	"(B) Primary annuitant.—For purposes
9	of subparagraph (A), the term 'primary annu-
10	itant' means the individual, the events in the
11	life of whom are of primary importance in af-
12	fecting the timing or amount of the payout
13	under the contract.
14	"(7) Treatment of changes in primary an-
15	NUITANT WHERE HOLDER OF CONTRACT IS NOT AN
16	INDIVIDUAL.—For purposes of this subsection, in
17	the case of a holder of an annuity contract which
18	is not an individual, if there is a change in a pri-
19	mary annuitant (as defined in paragraph (6)(B)),
20	such change shall be treated as the death of the
21	holder.
22	"(r) 10-Percent Additional Tax on Early Dis-
23	TRIBUTIONS FROM QUALIFIED RETIREMENT PLANS.—
24	"(1) Imposition of additional Tax.—If any
25	taxpayer receives any amount from a qualified re-

1	tirement plan (as defined in section 4974(c)), the
2	taxpayer's tax under this chapter for the taxable
3	year in which such amount is received shall be in-
4	creased by an amount equal to 10 percent of the
5	portion of such amount which is includible in gross
6	income.
7	"(2) Subsection not to apply to certain
8	DISTRIBUTIONS.—Except as provided in paragraphs
9	(3) and (4), paragraph (1) shall not apply to any of
10	the following distributions:
11	"(A) IN GENERAL.—Distributions which
12	are—
13	"(i) made on or after the date on
14	which the employee attains age 59½,
15	"(ii) made to a beneficiary (or to the
16	estate of the employee) on or after the
17	death of the employee,
18	"(iii) attributable to the employee's
19	being disabled within the meaning of sub-
20	section 72(m)(7) of the Internal Revenue
21	Code of 1986,
22	"(iv) part of a series of substantially
23	equal periodic payments (not less fre-
24	quently than annually) made for the life
25	(or life expectancy) of the employee or the

1	joint lives (or joint life expectancies) of
2	such employee and his designated bene-
3	ficiary,
4	"(v) made to an employee after sepa-
5	ration from service after attainment of age
6	55,
7	"(vi) dividends paid with respect to
8	stock of a corporation which are described
9	in section 404(k), or
10	"(vii) made from a Roth IRA (other
11	than a distribution described in section
12	30(d)(2)).
13	"(B) Medical expenses.—Distributions
14	made to the employee (other than distributions
15	described in subparagraph (A), (C), or (D)) to
16	the extent such distributions do not exceed the
17	amount allowable as a deduction under section
18	31 to the employee for amounts paid during the
19	taxable year for medical care (determined with-
20	out regard to whether the employee itemizes de-
21	ductions for such taxable year).
22	"(C) Payments to alternate payees
23	PURSUANT TO QUALIFIED DOMESTIC RELA-
24	TIONS ORDERS.—Any distribution to an alter-
25	nate payee pursuant to a qualified domestic re-

1	lations order (within the meaning of section
2	414(p)(1)).
3	"(D) Distributions to unemployed in-
4	DIVIDUALS FOR HEALTH INSURANCE PRE-
5	MIUMS.—
6	"(i) In general.—Distributions from
7	an individual retirement plan to an individ-
8	ual after separation from employment—
9	"(I) if such individual has re-
10	ceived unemployment compensation
11	for 12 consecutive weeks under any
12	Federal or State unemployment com-
13	pensation law by reason of such sepa-
14	ration,
15	"(II) if such distributions are
16	made during any taxable year during
17	which such unemployment compensa-
18	tion is paid or the succeeding taxable
19	year, and
20	"(III) to the extent such distribu-
21	tions do not exceed the amount paid
22	during the taxable year for insurance
23	described in section $213(d)(1)(D)$ of
24	the Internal Revenue Code of 1986

1	with respect to the individual and the
2	individual's spouse and dependents.
3	"(ii) Distributions after reem-
4	PLOYMENT.—Clause (i) shall not apply to
5	any distribution made after the individual
6	has been employed for at least 60 days
7	after the separation from employment to
8	which clause (i) applies.
9	"(iii) Self-employed individ-
10	UALS.—To the extent provided in regula-
11	tions, a self-employed individual shall be
12	treated as meeting the requirements of
13	clause (i)(I) if, under Federal or State law,
14	the individual would have received unem-
15	ployment compensation but for the fact the
16	individual was self-employed.
17	"(E) DISTRIBUTIONS FROM INDIVIDUAL
18	RETIREMENT PLANS FOR HIGHER EDUCATION
19	Expenses.—Distributions to an individual
20	from an individual retirement plan to the extent
21	such distributions do not exceed the qualified
22	higher education expenses (as defined in para-
23	graph (7)) of the taxpayer for the taxable year.
24	Distributions shall not be taken into account
25	under the preceding sentence if such distribu-

tions are described in subparagraph (A), (C), or

(D) or to the extent paragraph (1) does not
apply to such distributions by reason of subparagraph (B).

"(F) DISTRIBUTIONS FROM CERTAIN
PLANS FOR FIRST HOME PURCHASES.—Distributions to an individual from an individual
retirement plan which are qualified first-time
homebuyer distributions (as defined in paragraph (8)). Distributions shall not be taken into
account under the preceding sentence if such
distributions are described in subparagraph (A),
(C), (D), or (E) or to the extent paragraph (1)
does not apply to such distributions by reason
of subparagraph (B).

"(3) Limitations.—

"(A) CERTAIN EXCEPTIONS NOT TO APPLY TO INDIVIDUAL RETIREMENT PLANS.—Subparagraphs (A)(v), and (C) of paragraph (2) shall not apply to distributions from an individual retirement plan.

"(B) PERIODIC PAYMENTS UNDER QUALI-FIED PLANS MUST BEGIN AFTER SEPARA-TION.—Paragraph (2)(A)(iv) shall not apply to any amount paid from a trust described in sec-

1	tion 401(a) which is exempt from tax under
2	section 501(a) or from a contract described in
3	section 72(e)(5)(D)(ii) of the Internal Revenue
4	Code of 1986 unless the series of payments be-
5	gins after the employee separates from service.
6	"(4) Change in substantially equal pay-
7	MENTS.—
8	"(A) In general.—If—
9	"(i) paragraph (1) does not apply to
10	a distribution by reason of paragraph
11	(2)(A)(iv), and
12	"(ii) the series of payments under
13	such paragraph are subsequently modified
14	(other than by reason of death or disabil-
15	ity)—
16	"(I) before the close of the 5-year
17	period beginning with the date of the
18	first payment and after the employee
19	attains age $59\frac{1}{2}$, or
20	"(II) before the employee attains
21	age 59½, the taxpayer's tax for the
22	1st taxable year in which such modi-
23	fication occurs shall be increased by
24	an amount, determined under regula-
25	tions, equal to the tax which (but for

1	paragraph	(2)(A)(iv))	would	have
2	been impose	ed, plus intere	est for tl	ne de-
3	ferral period	d.		

- "(B) DEFERRAL PERIOD.—For purposes of this paragraph, the term 'deferral period' means the period beginning with the taxable year in which (without regard to paragraph (2)(A)(iv)) the distribution would have been includible in gross income and ending with the taxable year in which the modification described in subparagraph (A) occurs.
- "(5) EMPLOYEE.—For purposes of this subsection, the term 'employee' includes any participant, and in the case of an individual retirement plan, the individual for whose benefit such plan was established.
- "(6) Special rules for simple retirement account received from a simple retirement account (within the meaning of section 408(p) during the 2-year period beginning on the date such individual first participated in any qualified salary reduction arrangement maintained by the individual's employer under section 408(p)(2), paragraph (1) shall be applied by substituting '25 percent' for '10 percent'.

1	"(7) Qualified higher education ex-
2	PENSES.—For purposes of paragraph (2)(E)—
3	"(A) In general.—The term 'qualified
4	higher education expenses' means qualified
5	higher education expenses (as defined in section
6	10(b)(2)) for education furnished to—
7	"(i) the taxpayer,
8	"(ii) the taxpayer's spouse, or
9	"(iii) any child or grandchild of the
10	taxpayer or the taxpayer's spouse, at an el-
11	igible educational institution (as defined in
12	section $10(b)(2)(B)$).
13	"(B) Coordination with other provi-
14	SIONS.—For purposes of this subsection, sec-
15	tion 30 and section 32, qualified higher edu-
16	cation expenses in any taxable year shall be
17	treated as first paid with distributions under
18	section 32, next with distributions to which sec-
19	tion 30(d)(5)(v) (relating to early withdrawals
20	from Roth IRAs to pay higher education ex-
21	penses) applies, and finally from withdrawals to
22	which this subsection applies.
23	"(8) Qualified first-time homebuyer dis-
24	TRIBUTIONS.—For purposes of this subsection, the
25	term 'qualified first-time homebuyer distribution'

1 has the meaning given to it in section 30(d)(6) and 2 the limits contained in such section shall apply on a combined basis to this subsection and section 30. 3 Qualified acquisition costs (as defined in section 5 30(d)(6)) taken into account for purposes of section 6 30(d)(5)(vi) shall not also be taken into account sep-7 arately for purposes of this subsection. A taxpaver 8 may elect to treat distributions from an account 9 other than Roth IRAs to which this subsection ap-10 plies as a qualified first-time homeowner distribution 11 before determining whether a distribution from a 12 Roth IRAs is a qualified first-time homeowner dis-13 tribution.

14 "(r) 10-PERCENT ADDITIONAL TAX FOR TAXABLE 15 DISTRIBUTIONS FROM MODIFIED ENDOWMENT CON-16 TRACTS.—

"(1) Imposition of additional tax.—If any taxpayer receives any amount under a modified endowment contract (as defined in section 7702A), the taxpayer's tax under this chapter for the taxable year in which such amount is received shall be increased by an amount equal to 10 percent of the portion of such amount which is includible in gross income.

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1	"(2) Subsection not to apply to certain
2	DISTRIBUTIONS.—Paragraph (1) shall not apply to
3	any distribution—
4	"(A) made on or after the date on which
5	the taxpayer attains age 59½,
6	"(B) which is attributable to the tax-
7	payer's becoming disabled (within the meaning
8	of subsection (m)(7)), or
9	"(C) which is part of a series of substan-
10	tially equal periodic payments (not less fre-
11	quently than annually) made for the life (or life
12	expectancy) of the taxpayer or the joint lives
13	(or joint life expectancies) of such taxpayer and
14	his beneficiary.
15	"Subchapter C—Basis, Business Transactions
16	and Nonrecognition Transactions
	"Sec. 71. Gain or loss on the sale of an asset.
	"Sec. 72. Basis. "Sec. 73. Basis in business entities. "Sec. 74. Gratuitous transfers. "Sec. 75. Transactions involving business entities. "Sec. 76. Rollover on residence sale. "Sec. 77. Other nonrecognition transactions. "Sec. 78. Wash sales and straddles.
17	"Sec. 73. Basis in business entities. "Sec. 74. Gratuitous transfers. "Sec. 75. Transactions involving business entities. "Sec. 76. Rollover on residence sale. "Sec. 77. Other nonrecognition transactions.
17 18	"Sec. 73. Basis in business entities. "Sec. 74. Gratuitous transfers. "Sec. 75. Transactions involving business entities. "Sec. 76. Rollover on residence sale. "Sec. 77. Other nonrecognition transactions. "Sec. 78. Wash sales and straddles.
	 "Sec. 73. Basis in business entities. "Sec. 74. Gratuitous transfers. "Sec. 75. Transactions involving business entities. "Sec. 76. Rollover on residence sale. "Sec. 77. Other nonrecognition transactions. "Sec. 78. Wash sales and straddles. "SEC. 71. GAIN OR LOSS ON THE SALE OF AN ASSET.
18	"Sec. 73. Basis in business entities. "Sec. 74. Gratuitous transfers. "Sec. 75. Transactions involving business entities. "Sec. 76. Rollover on residence sale. "Sec. 77. Other nonrecognition transactions. "Sec. 78. Wash sales and straddles. "Sec. 71. GAIN OR LOSS ON THE SALE OF AN ASSET. "(a) IN GENERAL.—Except as otherwise provided in

1	"(1) the amount realized from the disposition,
2	over
3	"(2) the taxpayer's adjusted basis in the prop-
4	erty.
5	"(b) Amount Realized.—The amount realized from
6	the disposition of property shall be sum of money received
7	plus the fair market value of the property (other than
8	money) received. See section 122(c) for the treatment of
9	installment sales.
10	"(c) Nonrecognition Transaction.—Subsection
11	(a) shall not apply to nonrecognition transactions de-
12	scribed in this chapter.
13	"(d) Contracts Marked to Market.—
14	"(1) In general.—Under regulations pre-
15	scribed by the Secretary, a markable contract held
16	by the taxpayer at the end of the year shall be treat-
17	ed as sold and reacquired for its fair market value
18	on the last business day of the taxable year. The
19	regulations shall adopt principles and definitions
20	similar to those that applied under section 1256 of
21	the Internal Revenue Code of 1986.
22	"(2) Markable contract.—For purposes of
23	this subsection, 'markable contract' means—
24	"(A) any regulated futures contract,
25	"(B) any foreign currency contract,

1	"(C) any nonequity option,
2	"(D) any dealer equity option
3	as such terms were defined for purposes of section
4	1256 of the Internal Revenue Code of 1986.
5	"SEC. 72. BASIS.
6	"(a) Basis, Sale, or Exchange.—Except to the ex-
7	tent inconsistent with provisions of this chapter, adjusted
8	basis and the existence of a sale or exchange shall be de-
9	termined in accordance with principles applicable under
10	the Internal Revenue Code of 1986.
11	"(b) Definition of Basis.—For purposes of this
12	chapter, 'basis' means the adjusted basis of property. The
13	adjusted basis of property is generally its cost, as adjusted
14	for actions or transactions that increase or decrease the
15	basis of property. Except as provided in section 73 (relat-
16	ing to business entities and basis in business entities), the
17	taxpayer's adjusted basis on January 1, 1999, in an asset
18	acquired before that date, shall be its adjusted basis as
19	of December 31, 1998, as determined under the Internal
20	Revenue Code of 1986.
21	"SEC. 73. BASIS IN BUSINESS ENTITIES.
22	"(a) Rules for All Business Entities.—
23	"(1) In general.—A taxpayer's basis in an in-
24	terest in a business entity shall equal—
25	"(A) the cost of acquiring the interest.

1	"(B) increased by the amount of cash and
2	basis of any property contributed to the entity,
3	and
4	"(C) decreased by the portion of any liq-
5	uidating distributions from the entity that are
6	treated as returns of capital in accordance with
7	rules prescribed by the Secretary.
8	"(2) Initial basis.—Except as otherwise pro-
9	vided in this section, a taxpayer's basis on January
10	1, 1999, or any interest in a business entity held as
11	of December 31, 1998, shall be the basis of such in-
12	terest as of December 31, 1998, as determined
13	under the Internal Revenue Code of 1986.
14	"(3) Cross references.—See section 75 for
15	rules relating to the effect of certain business trans-
16	actions on a taxpayer's basis.
17	"(4) Special rule for contribution of
18	PERSONAL USE PROPERTY.—If a taxpayer contrib-
19	utes personal-use property (as defined in section
20	210(b)(3)(B)), the taxpayer's basis in the property
21	shall not be increased by an amount in excess of the
22	fair market value of the property contributed.
23	"(b) Special Rules for Partnership Inter-
24	ESTS.—

1	"(1) Initial basis in old partnerships.—A
2	partner's basis in a partnership interest as of Janu-
3	ary 1, 1999, equals—
4	"(A) the partner's basis in the partnership
5	as of the end of the taxable year ending on De-
6	cember 31, 1998, minus
7	"(B) the amount of the partner's share of
8	the indebtedness of the partnership taken into
9	account in determining such basis.
10	"(2) Negative basis.—If the amount deter-
11	mined under paragraph (1) is negative, the taxpayer
12	has a negative basis in the partnership and such
13	negative basis shall increase the gain on the sale or
14	disposition of the partnership interest (except to the
15	extent such negative basis has been adjusted by rea-
16	son of capital contributions).
17	"(3) Adjustment to basis.—Except as other-
18	wise provided in this section, a partner's basis in a
19	partnership interest shall be determined in accord-
20	ance with the general principles of this chapter ap-
21	plicable to an individual's basis in an interest in a
22	business entity. A partner's basis in a partnership
23	shall not be adjusted by reason of any—
24	"(A) distribution from the partnership (ex-
25	cept to the extent such distribution is treated as

1	distribution of basis in accordance with the gen-
2	eral principles of this chapter applicable to an
3	individual's basis in an interest in a business
4	entity),
5	"(B) income, earnings, or loss of the part-
6	nership, or
7	"(C) any change in the partner's share of
8	the partnership's indebtedness.
9	"(4) Special rule for transition distribu-
10	TIONS.—
11	"(A) EFFECT OF TRANSITION DISTRIBU-
12	TION.—A transition distribution from partner-
13	ship to a partner shall—
14	"(i) reduce the partner's basis in the
15	partnership, and
16	"(ii) not be included in gross income.
17	"(B) Definition.—A 'transition distribu-
18	tion' is a distribution by a business entity to an
19	individual made during the first three months
20	of 1999 but only to the extent that such dis-
21	tribution, when added to all other distributions
22	of the entity to the individual after March 31,
23	1998, does not exceed the amount of taxable in-
24	come allocated by the entity to the individual

1	during the taxable year of the entity ending on
2	December 31, 1998.
3	"(5) Partnership.—For purposes of this sec-
4	tion, 'partnership' includes a limited liability com-
5	pany that was taxable as a partnership under the
6	Internal Revenue Code of 1986.
7	"(c) Special Rules for Shares of S Corpora-
8	TIONS.—Rules similar to those contained in subsection (b)
9	shall apply with respect to the basis of stock of a corpora-
10	tion that was treated as an S corporation under the Inter-
11	nal Revenue Code of 1986.
12	"(d) Special Rules for Proprietorships.—
13	"(1) OLD PROPRIETORSHIP.—A proprietor's
14	basis in any business activity conducted before Janu-
15	ary 1, 1999, which is treated as a business activity
16	as of such date equals—
17	"(A) the proprietor's adjusted basis in the
18	assets of such business entity as of the end of
19	the taxable year ending on December 31, 1998,
20	minus
21	"(B) the balance of any indebtedness the
22	interest on which the proprietor had treated as
23	business interest under section $163(h)(2)(A)$ of
24	the Internal Revenue Code of 1986.

1	"(2) Negative basis.—If the amount deter-
2	mined under paragraph (1) is negative, the propri-
3	etor has a negative basis in the proprietorship and
4	such negative basis shall increase the gain on the
5	sale or disposition of the entity (except to the extent
6	such negative basis has been adjusted by reason of
7	capital contributions).
8	"(3) Adjustment to basis.—Except as other-
9	wise provided in this section, a proprietor's basis in
10	a proprietorship shall be determined in accordance
11	with the general principles of this chapter applicable
12	to an individual's basis in an interest in a business
13	entity.
14	"(4) Proprietorship'
15	includes—
16	"(A) any family business that is not a
17	partnership, and
18	"(B) any business activity conducted by a
19	taxpayer other than as an employee if such ac-
20	tivity constitutes a business entity.
21	"(e) Anti-Avoidance Rule.—
22	"(1) In general.—If a pass-through entity's
23	distributions to an individual in its taxable year or
24	taxable years ending in 1998 exceeds 125 percent of
25	the individual's distributive share of income for such

- 1 period, the amount of such excess distribution shall
- 2 be treated as a cash distribution to the partner on
- 3 January 1, 1999, and shall not reduce the partner's
- 4 basis in his partnership interest.
- 5 "(2) Pass through entity.—'Pass through
- 6 entity' means a partnership, proprietorship, or S
- 7 corporation.

8 "SEC. 74. GRATUITOUS TRANSFERS.

- 9 "(a) IN GENERAL.—If after December 31, 1998, a
- 10 taxpayer receives any property by gift, inheritance, or
- 11 other gratuitous transfer, the taxpayer's basis in the prop-
- 12 erty shall be the lesser of—
- "(1) the fair market value of the property at
- the time of transfer, or
- 15 "(2) the transferee's basis in the property at
- the time of transfer.
- 17 "(b) Proof Required.—A taxpayer's basis in an
- 18 asset received by gift, inheritance, or other gratuitous
- 19 transfer shall be presumed to be zero unless the taxpayer
- 20 can demonstrate to the satisfaction of the Secretary the
- 21 basis claimed by the taxpayer.
- 22 "SEC. 75. DISTRIBUTIONS FROM BUSINESS ENTITIES.
- 23 "(a) IN GENERAL.—Except as otherwise provided in
- 24 this section or in regulations issued by the Secretary in
- 25 accordance with this section—

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- "(1) Cash distributions.—Distributions of cash by a business entity with respect to its equity ownership shall be treated as dividends and included in gross income.
 - "(2) DISTRIBUTIONS OF PROPERTY.—If a business entity distributes property (other than stock or other equity ownership described in paragraph (3) in connection with a merger, acquisition or reorganization), the fair market value of the property received shall be treated as a dividend and included in gross income.
 - "(3) DISTRIBUTIONS OF STOCK OR OTHER EQ-UITY OWNERSHIP.—If a taxpayer receives with respect to its ownership interest in a business entity stock or other ownership interests in such business entity (as reorganized) or in another business entity that is controlled by such business entity or is acquiring or merging with such business entity, no gain or loss shall be recognized on the distribution.
- "(b) Basis in Business Divisions.—In the case of 21 a spin-off, split-off, or split-up of a business entity in 22 which a taxpayer has basis, the taxpayer's basis in the 23 original business entity shall be allocated among the new 24 and surviving entities in accordance with the relative fair 25 market values of the taxpayer's interests in those entities.

- 1 If interests in the entities are publicly traded, fair market
- 2 values shall be based on public trading prices. In other
- 3 cases, the Secretary shall accept any reasonable allocation
- 4 made by the taxpayer if the taxpayer notifies the Secretary
- 5 of the allocation in an attachment to its tax return for
- 6 the taxable year of the transaction.
- 7 "(c) Distributions Constituting Return of
- 8 Basis.—

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"(1) Complete Liquidations.—

"(A) IN GENERAL.—In the case of a distribution in complete liquidation of a business entity, a taxpayer shall be treated as receiving cash and assets of the entity in exchange for the taxpayer's equity in the business entity. In such case, the taxpayer shall recognize gain to the extent that the sum of the cash and fair market value of assets received exceeds the taxpayer's basis in its interest in the business entity or shall recognize loss to the extent that the basis exceeds the fair market value of cash and assets received.

"(B) DISTRIBUTION OF EQUITY INTER-ESTS.—In the case of a complete liquidation in which at least 90 percent of the value of assets and cash distributed to an equity holder is eq-

1	uity interests in other business entities con-
2	trolled by the distributing entity—
3	"(i) subparagraph (A) shall not apply,
4	"(ii) paragraph (3) of subsection (a)
5	shall apply,
6	"(iii) the cash and fair market value
7	of assets other than equity interests in
8	controlled entities shall be applied to re-
9	duce the taxpayer's basis in the distribut-
10	ing entity and gain will be recognized only
11	to the extent that the cash and such fair
12	market value exceeds the taxpayer's basis
13	in the distributing entity, and
14	"(iv) the taxpayer's remaining basis
15	shall be allocated among the distributed
16	equity interests in controlled entities in ac-
17	cordance with the relative fair market val-
18	ues of such interests.
19	"(C) Distribution of Business Prop-
20	ERTY.—Under regulations prescribed by the
21	Secretary, rules similar to those that applied to
22	partnerships under the Internal Revenue Code
23	of 1986 shall apply in lieu of subparagraph (A)
24	to distributions that include property used in a
25	trade or business if such property is contributed

1	to a new business entity within 180 days of the
2	distribution.
3	"(2) Transition rules.—See subsections (b)
4	and (d) of section 73 for transition rules relating to
5	partnerships and proprietorships.
6	"(c) Definitions and Special Rules.—
7	"(1) CERTAIN RULES OF APPLICATION.—
8	"(A) Principles applicable to inter-
9	NAL REVENUE CODE.—This section shall be ap-
10	plied without regard to—
11	"(i) continuity of business interest,
12	"(ii) continuity of ownership interest,
13	"(iii) requirements of section 355 of
14	the Internal Revenue Code of 1986 for
15	spin-offs, split-offs and split-ups,
16	"(iv) business purposes for a cor-
17	porate reorganization or restructuring (ex-
18	cept if the transaction is potentially abu-
19	sive), and
20	"(v) except as provided in paragraph
21	(3), rules treating dividends as returns of
22	capital because of the absence of earnings
23	and profits.
24	"(B) Constructive receipt.—If a tax-
25	payer is given the choice of receiving cash or an

1	equity interest in a business entity, the tax-
2	payer will be treated for purposes of this sec-
3	tion as if he received the cash and purchased
4	the equity interest.
5	"(C) Debt versus equity.—The prin-
6	ciples distinguishing debt and equity that ap-
7	plied prior to the adopt of the Simplified USA
8	Tax generally shall apply for purposes of apply-
9	ing this section. An investment in a business
10	entity shall not be considered debt unless—
11	"(i) it is reflected in the books and
12	records of the business entity as debt, and
13	"(ii) there is written evidence of the
14	investment that treats such investment as
15	indebtedness.
16	"(2) Control.—For purposes of this section,
17	'control' of a business entity means—
18	"(A) ownership of more than 50% of the
19	voting power held by equity holders of such en-
20	tity, or
21	"(B) ownership of rights to more than
22	50% of the periodic distributions that the busi-
23	ness entity may make to its equity holders and
24	50% of the distributions if the business entity
25	were liquidated.

1	"(3) Regulations.—
2	"(A) Significant downsizing and par-
3	TIAL LIQUIDATIONS.—The Secretary is author-
4	ized to issue regulations under which distribu-
5	tions resulting from a significant downsizing of
6	a business entity will be treated in part as re-
7	turn of equity holders' capital.
8	"(B) Assumption and release of li-
9	ABILITY.—The Secretary shall prescribe regula-
10	tions addressing the consequences of a
11	distributee's assumption of the liabilities of the
12	distributor.
13	"SEC. 76. EXCLUSION OF GAIN FROM SALE OF PRINCIPAL
1314	"SEC. 76. EXCLUSION OF GAIN FROM SALE OF PRINCIPAL RESIDENCE.
14 15	RESIDENCE.
141516	residence. "(a) Exclusion.—Gross income shall not include
14151617	RESIDENCE. "(a) Exclusion.—Gross income shall not include gain from the sale or exchange of property if, during the
14151617	residence. "(a) Exclusion.—Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale or exchange,
14 15 16 17 18	"(a) EXCLUSION.—Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer
141516171819	"(a) Exclusion.—Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as the taxpayer's principal residence for periods aggregat-
14 15 16 17 18 19 20	"(a) EXCLUSION.—Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as the taxpayer's principal residence for periods aggregating 2 years or more.
14 15 16 17 18 19 20 21	"(a) Exclusion.—Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as the taxpayer's principal residence for periods aggregating 2 years or more. "(b) Limitations.—
14 15 16 17 18 19 20 21 22	"(a) Exclusion.—Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale or exchange, such property has been owned and used by the taxpayer as the taxpayer's principal residence for periods aggregating 2 years or more. "(b) Limitations.— "(1) In General.—The amount of gain ex-

1	"(2) $$500,000$ limitation for certain joint
2	RETURNS.—Paragraph (1) shall be applied by sub-
3	stituting '\$500,000' for '\$250,000' if—
4	"(A) a husband and wife make a joint re-
5	turn for the taxable year of the sale or ex-
6	change of the property,
7	"(B) either spouse meets the ownership re-
8	quirements of subsection (a) with respect to
9	such property,
10	"(C) both spouses meet the use require-
11	ments of subsection (a) with respect to such
12	property, and
13	"(D) neither spouse is ineligible for the
14	benefits of subsection (a) with respect to such
15	property by reason of paragraph (3).
16	"(3) Application to only 1 sale or ex-
17	CHANGE EVERY 2 YEARS.—
18	"(A) In general.—Subsection (a) shall
19	not apply to any sale or exchange by the tax-
20	payer if, during the 2-year period ending on the
21	date of such sale or exchange, there was any
22	other sale or exchange by the taxpayer to which
23	subsection (a) applied.
24	"(B) Pre-may 7, 1997, sales not taken
25	INTO ACCOUNT.—Subparagraph (A) shall be

1	applied without regard to any sale or exchange
2	before May 7, 1997.
3	"(c) Exclusion for Taxpayers Failing To Meet
4	CERTAIN REQUIREMENTS.—
5	"(1) In general.—In the case of a sale or ex-
6	change to which this subsection applies, the owner-
7	ship and use requirements of subsection (a) shall not
8	apply and subsection (b)(3) shall not apply; but the
9	amount of gain excluded from gross income under
10	subsection (a) with respect to such sale or exchange
11	shall not exceed—
12	"(A) the amount which bears the same
13	ratio to the amount which would be so excluded
14	under this section if such requirements had
15	been met, as
16	"(B) the shorter of—
17	"(i) the aggregate periods, during the
18	5-year period ending on the date of such
19	sale or exchange, such property has been
20	owned and used by the taxpayer as the
21	taxpayer's principal residence, or
22	"(ii) the period after the date of the
23	most recent prior sale or exchange by the
24	taxpayer to which subsection (a) applied

1	and before the date of such sale or ex-
2	change,
3	bears to 2 years.
4	"(2) Sales and exchanges to which sub-
5	SECTION APPLIES.—This subsection shall apply to
6	any sale or exchange if—
7	"(A) subsection (a) would not (but for this
8	subsection) apply to such sale or exchange by
9	reason of—
10	"(i) a failure to meet the ownership
11	and use requirements of subsection (a), or
12	"(ii) subsection (b)(3), and
13	"(B) such sale or exchange is by reason of
14	a change in place of employment, health, or, to
15	the extent provided in regulations, unforeseen
16	circumstances.
17	"(d) Special Rules.—
18	"(1) Joint returns.—If a husband and wife
19	make a joint return for the taxable year of the sale
20	or exchange of the property, subsections (a) and (c)
21	shall apply if either spouse meets the ownership and
22	use requirements of subsection (a) with respect to
23	such property.
24	"(2) Property of Deceased Spouse.—For
25	purposes of this section, in the case of an unmarried

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individual whose spouse is deceased on the date of the sale or exchange of property, the period such unmarried individual owned and used such property shall include the period such deceased spouse owned and used such property before death.

- "(3) Property owned by spouse or former spouse.—For purposes of this section—
 - "(A) PROPERTY TRANSFERRED TO INDI-VIDUAL FROM SPOUSE OR FORMER SPOUSE.— In the case of an individual holding property transferred to such individual by such individual's spouse or former spouse in a transaction incident to divorce, the period such individual owns such property shall include the period the transferor owned the property.
 - "(B) PROPERTY USED BY FORMER SPOUSE
 PURSUANT TO DIVORCE DECREE, ETC.—Solely
 for purposes of this section, an individual shall
 be treated as using property as such individual's principal residence during any period of
 ownership while such individual's spouse or
 former spouse is granted use of the property
 under a divorce or separation instrument.
- "(4) Tenant-stockholder in cooperative housing corporation.—For purposes of this sec-

1	tion, if the taxpayer holds stock as a tenant-stock-
2	holder in a cooperative housing corporation—
3	"(A) the holding requirements of sub-
4	section (a) shall be applied to the holding of
5	such stock, and
6	"(B) the use requirements of subsection
7	(a) shall be applied to the house or apartment
8	which the taxpayer was entitled to occupy as
9	such stockholder.
10	"(5) Involuntary conversions.—For pur-
11	poses of this section, the destruction, theft, seizure,
12	requisition, or condemnation of property shall be
13	treated as the sale of such property.
14	"(6) Determination of use during periods
15	OF OUT-OF-RESIDENCE CARE.—In the case of a tax-
16	payer who—
17	"(A) becomes physically or mentally in-
18	capable of self-care, and
19	"(B) owns property and uses such property
20	as the taxpayer's principal residence during the
21	5-year period described in subsection (a) for pe-
22	riods aggregating at least 1 year,
23	then the taxpayer shall be treated as using such
24	property as the taxpayer's principal residence during
25	any time during such 5-year period in which the tax-

1	payer owns the property and resides in any facility
2	(including a nursing home) licensed by a State or
3	political subdivision to care for an individual in the
4	taxpayer's condition.
5	"(7) Sales of remainder interests.—For
6	purposes of this section—
7	"(A) IN GENERAL.—At the election of the
8	taxpayer, this section shall not fail to apply to
9	the sale or exchange of an interest in a prin-
10	cipal residence by reason of such interest being
11	a remainder interest in such residence, but this
12	section shall not apply to any other interest in
13	such residence which is sold or exchanged sepa-
14	rately.
15	"(B) Exception for sales to related
16	PARTIES.—Subparagraph (A) shall not apply to
17	any sale to, or exchange with, a related party
18	(as defined in section 171).
19	"(e) Denial of Exclusion for Expatriates.—
20	This section shall not apply to any sale or exchange by
21	an individual if rules relating to expatriation to avoid tax
22	apply to such individual.
23	"(f) Election To Have Section Not Apply.—
24	This section shall not apply to any sale or exchange with

- 1 respect to which the taxpayer elects not to have this sec-
- 2 tion apply.
- 3 "(g) Residences Acquired in Rollovers Under
- 4 Section 1034.—For purposes of this section, in the case
- 5 of property the acquisition of which by the taxpayer re-
- 6 sulted under section 1034 of the Internal Revenue Code
- 7 of 1986 (as in effect on the day before the date of the
- 8 enactment of the Taxpayer Relief Act of 1997) in the non-
- 9 recognition of any part of the gain realized on the sale
- 10 or exchange of another residence, in determining the pe-
- 11 riod for which the taxpayer has owned and used such
- 12 property as the taxpayer's principal residence, there shall
- 13 be included the aggregate periods for which such other
- 14 residence (and each prior residence taken into account in
- 15 determining the holding period of such property) had been
- 16 so owned and used.

17 "SEC. 77. OTHER NONRECOGNITION TRANSACTIONS.

- 18 "(a) Involuntary Conversions.—Under regula-
- 19 tions prescribed by the Secretary, the involuntary conver-
- 20 sion of property held by an individual shall not result in
- 21 gross income to the individual to the extent that the indi-
- 22 vidual receives property in exchange for the involuntarily
- 23 converted property. To the extent that income is not rec-
- 24 ognized under this subsection, the taxpayer's basis in the
- 25 converted property shall carry over to the new property.

1	"(b) Certain Reacquisitions of Real Prop-
2	ERTY.—Under regulations prescribed by the Secretary,
3	gross income shall not be recognized in the case of certain
4	reacquisitions of real property. The regulations shall adopt
5	principles similar to those under section 1038 of the Inter-
6	nal Revenue Code of 1986.
7	"(c) Transfers of Property Between Spouses
8	OR INCIDENT TO DIVORCE.—
9	"(1) General Rule.—Gross income shall not
10	be recognized on the transfer of property from an
11	individual to (or in trust for the benefit of)—
12	"(A) a spouse, or
13	"(B) a former spouse, but only if the
14	transfer is incident to divorce.
15	"(2) Transfer treated as a gift.—
16	Any transfer described in paragraph (1) shall
17	be treated as a gift.
18	"(d) Certain Exchanges of Insurance Poli-
19	CIES.—Under regulations prescribed by the Secretary,
20	gross income shall not be recognized on the exchange of
21	insurance policies or another life insurance policy or an
22	annuity contract or the exchange of annuity contracts
23	The regulations shall adopt principles similar to those

24 under section 1035 of the Internal Revenue Code of 1986.

- 1 "(e) CERTAIN EXCHANGES OF UNITED STATES OB-
- 2 LIGATIONS.—When so provided by regulations promul-
- 3 gated by the Secretary in connection with the issue of obli-
- 4 gations of the United States, no gain or loss shall be rec-
- 5 ognized on the surrender to the United States of obliga-
- 6 tions of the United States issued under chapter 31 of title
- 7 31 in exchange solely for other obligations issued under
- 8 such chapter.

9 "SEC. 78. WASH SALES AND STRADDLES.

- 10 "(a) Losses From Wash Sales of Stock or Se-
- 11 Curities.—Under regulations prescribed by the Sec-
- 12 retary, no loss shall be recognized on the wash sale of
- 13 stock or securities. The regulations shall adopt principles
- 14 similar to those under section 1091 of the Internal Reve-
- 15 nue Code of 1986.
- 16 "(b) Straddles.—Under regulations prescribed by
- 17 the Secretary, the loss that can be taken into account from
- 18 1 or more straddle positions shall be limited. The regula-
- 19 tions shall adopt principles similar to those under section
- 20 1038 of the Internal Revenue Code of 1986.
- 21 "SEC. 79. LIMITATION ON LOSSES FROM CAPITAL TRANS-
- ACTIONS.
- 23 "(a) No Loss on Personal Use Property.—No
- 24 loss shall be recognized on the sale or exchange of personal
- 25 use property (as defined in section 210(b)(3)(B)).

"(b) Limitation on Net Capital Loss.—

- "(1) IN GENERAL.—Losses from sales or exchanges of capital assets in a taxable year shall be allowed only to the extent of the gains from such sales or exchanges, plus \$3,000 (\$1,500 in the case of a married individual filing a separate return).
 - "(2) Capital loss carryovers.—Under regulations prescribed by the Secretary, any loss not allowed by reason of paragraph (1) shall be carried over to the following taxable year and treated as a capital loss incurred in such year. There shall be no limit on the number of years that a capital loss can be carried forward.
 - "(3) Capital assets.—Under regulations prescribed by the Secretary, the principles of the Internal Revenue Code of 1986 (including, without limitation, sections 1234 (relating to options), 1234A (relating to gains or losses from certain terminations), 1253 (relating to franchises and trademarks) and 1258 (gain from certain financial transactions) shall apply for purposes of determining what is a capital asset and whether an event is to be treated as a sale or exchange of capital assets, except to the extent inconsistent with principles of this chapter.

"(4) RECAPTURE.—If a taxpayer claimed de-1 2 preciation, amortization or other cost recovery deductions under the Internal Revenue Code of 1986 3 with respect to property which is subsequently sold or exchanged in a transactions that is not treated as 6 transaction of a business entity, the amount of gain 7 on the exchange of such property which is treated as 8 gain from the sale or exchange of a capital asset 9 shall be reduced (but not below zero) by the amount 10 of such deductions claimed with respect to the prop-11 erty.

12 "Subchapter D—Rules for Exclusions from

13 Gross Income

14 "SEC. 91. INTEREST ON TAX-EXEMPT BONDS.

- 15 "(a) Exclusion.—Except as provided in subsection
- 16 (b), gross income does not include interest on any State
- 17 or local bond.
- 18 "(b) Exceptions.—Subsection (a) shall not apply
- 19 to—
- 20 "(1) Private activity bond which is not a
- 21 QUALIFIED BOND—Any private activity bond which

[&]quot;Sec. 91. Interest on tax-exempt bonds.

[&]quot;Sec. 92. Combat pay.

[&]quot;Sec. 93. Qualified military benefits.

[&]quot;Sec. 94. Qualified foster care payments.

[&]quot;Sec. 95. Compensation for injury and sickness.

[&]quot;Sec. 96. Meals or lodging for convenience of employer.

[&]quot;Sec. 97. Certain fringe benefits.

1	is not a qualified bond (within the meaning of para-
2	graph (3) of subsection (e)).
3	"(2) Arbitrage bond.—Any arbitrage bond.
4	"(3) Bond not in registered form, etc.—
5	Any bond unless such bond meets the applicable re-
6	quirements set forth in regulations.
7	"(c) Definitions—For purposes of this section—
8	"(1) State or local bond.—'State or local
9	bond' means an obligation of a State or political
10	subdivision thereof.
11	"(2) State.—'State' includes the District of
12	Columbia and any possession of the United States.
13	"(3) Qualified bond.—"Qualified bond"
14	MEANS ANY PRIVATE ACTIVITY BOND IF—
15	"(A) In general.—Such bond is—
16	"(i) an exempt facility bond,
17	"(ii) a qualified mortgage bond,
18	"(iii) a qualified veterans' mortgage
19	bond,
20	"(iv) a qualified small issue bond,
21	"(v) a qualified student loan bond,
22	"(vi) a qualified 253(c)(3) bond.
23	"(B) VOLUME CAP.—Such bond is issued
24	as part of an issue which meets the applicable

1	volume cap requirements set forth in regula-
2	tions.
3	"(C) Other requirements.—Such bond
4	meets the applicable requirements set forth in
5	regulations.
6	"(d) Regulations.—
7	"(1) STATUTORY REGULATIONS.—The Sec-
8	retary shall publish as regulations governing the ap-
9	plication of this section the text of part IV of sub-
10	chapter B of chapter 1 of the Internal Revenue Code
11	of 1986 (sections 141 through 149) with only such
12	changes as are required to conform cross references.
13	"(2) OTHER REGULATIONS.—The Secretary
14	shall have the authority to promulgate such other
15	regulations as he deems necessary or proper to im-
16	plement this section, except that no such regulations
17	shall conflict with the regulations mandated by para-
18	graph (1) except as provided in this subtitle.
19	"SEC. 92. COMBAT PAY.
20	"(a) Enlisted Personnel.—Gross income does not
21	include compensation received for active service as a mem-
22	ber below the grade of commissioned officer in the Armed
23	Forces of the United States for any month during any
24	part of which such member—
25	"(1) served in a combat zone, or

1	"(2) was hospitalized as a result of wounds, dis-
2	ease, or injury incurred while serving in a combat
3	zone; but this paragraph shall not apply for any
4	month beginning more than 2 years after the date
5	of the termination of combatant activities in such
6	zone.
7	"(b) Commissioned Officers.—Gross income does
8	not include so much of the compensation as does not ex-
9	ceed \$500 received for active service as a commissioned
10	officer in the Armed Forces of the United States for any
11	month during any part of which such officer—
12	"(1) served in a combat zone, or
13	"(2) was hospitalized as a result of wounds, dis-
14	ease, or injury incurred while serving in a combat
15	zone; but this paragraph shall not apply for any
16	month beginning more than 2 years after the date
17	of the termination of combatant activities in such
18	zone.
19	"(c) Definitions.—For purposes of this section—
20	"(1) 'Commissioned officer' does not include a
21	commissioned warrant officer.
22	"(2) 'Combat zone' means any area which the
23	President of the United States by Executive Order
24	designates, for purposes of this section or cor-

responding provisions of prior income tax laws, an

- area in which Armed Forces of the United States are or have (after June 24, 1950) engaged in combat.
- "(3) Service is performed in a combat zone only 5 if performed on or after the date designated by the 6 President by Executive Order as the date of the commencing of combatant activities in such zone, 7 8 and on or before the date designated by the Presi-9 dent by Executive Order as the date of the termi-10 nation of combatant activities in such zone; except 11 that June 25, 1950, shall be considered the date of 12 the commencing of combatant activities in the com-13 bat zone designated in Executive Order 10195.
- 14 "(4) The term 'compensation' does not include 15 pensions and retirement pay.

16 "SEC. 93. QUALIFIED MILITARY BENEFIT.

- 17 "(a) IN GENERAL.—'Qualified military benefit' 18 means any allowance or in-kind benefit (other than per-19 sonal use of a vehicle) which—
- 20 "(1) is received by any member or former mem-21 ber of the uniformed service of the United States or 22 any dependent of such member by reason of such 23 member's status or service as a member of such uni-

1	"(2) was excludable from gross income on Sep-
2	tember 9, 1986, under any provision of law, regula-
3	tion, or administrative practice which was in effect
4	on such date (other than a provision of this title).
5	"(b) No Other Benefit To Be Excludable as
6	PROVIDED BY THIS TITLE.—Notwithstanding any other
7	provision of law, no benefit shall be treated as a qualified
8	military benefit unless such benefit—
9	"(1) is a benefit described in subsection (a), or
10	"(2) is excludable from gross income under this
11	title without regard to any provision of law which is
12	not contained in this title and which is not contained
13	in a revenue Act.
14	"(c) Limitations on Modifications.—
15	"(1) In general.—Except as provided in para-
16	graph (2), no modification or adjustment of any
17	qualified military benefit after September 9, 1986,
18	shall be taken into account.
19	"(2) Exception for certain adjustments
20	TO CASH BENEFITS.—Paragraph (1) shall not apply
21	to any adjustment to any qualified military benefit
22	payable in cash which—
23	"(A) is pursuant to a provision of law or
24	regulation (as in effect on September 9, 1986),
25	and

1	"(B) is determined by reference to any
2	fluctuation in cost, price, currency, or other
3	similar index.
4	"SEC. 94. QUALIFIED FOSTER CARE PAYMENTS.
5	"(a) Qualified Foster Care Payment De-
6	FINED.—
7	"(1) In general.—'Qualified foster care pay-
8	ment' means any amount—
9	"(A) which is paid by a state or political
10	subdivision thereof or by a placement agency
11	which is described in section 253(c)(3) and ex-
12	empt from tax under section 253(a), and
13	"(B) which is—
14	"(i) paid to the foster care provider
15	for caring for a qualified foster individual
16	in the foster care provider's home, or
17	"(ii) a difficulty of care payment.
18	"(2) Qualified foster individual.—"Quali-
19	fied foster individual' means any individual who is
20	living in a foster family home in which such individ-
21	ual was placed by—
22	"(A) an agency of a State or a political
23	subdivision thereof, or
24	"(B) in the case of an individual who has
25	not attained age 19, an organization which is li-

1	censed by a State (or political subdivision there-
2	of) as a placement agency and which is de-
3	scribed in section 253(c)(3) and exempt from
4	tax under section 253(a).
5	"(3) Limitation based on number of indi-
6	VIDUALS OVER THE AGE OF 18.—In the case of any
7	foster home in which there is a qualified foster care
8	individual who has attained age 19, foster care pay-
9	ments (other than difficulty of care payments) for
10	any period to which such payments relate shall not
11	be excludable from gross income under subsection
12	(a) to the extent such payments are made for more
13	than 5 such qualified foster individuals.
14	"(b) Difficulty of Care Payments.—For pur-
15	poses of this section—
16	"(1) Difficulty of care payments.—'Dif-
17	ficulty of care payments' means payments to individ-
18	uals which are not described in subsection
19	(a)(1)(B)(i), and which—
20	"(A) are compensation for providing the
21	additional care of a qualified foster individual
22	which is—
23	"(i) required by reason of a physical,
24	mental, or emotional handicap of such in-
25	dividual with respect to which the State

1	has determined that there is a need for ad-
2	ditional compensation, and
3	"(ii) provided in the home of the fos-
4	ter care provider, and
5	"(B) are designated by the payor as com-
6	pensation described in subparagraph (A).
7	"(2) Limitation based on number of indi-
8	VIDUALS.—In the case of any foster home, difficulty
9	of care payments for any period to which such pay-
10	ments relate shall not be excludable from gross in-
11	come under subsection (a) to the extent such pay-
12	ments are made for more than—
13	"(A) 10 qualified foster individuals who
14	have not attained age 19, and
15	"(B) 5 qualified foster individuals not de-
16	scribed in subparagraph (A).
17	"SEC. 95. COMPENSATION FOR INJURIES OR SICKNESS.
18	"(a) In General.—Gross income does not include—
19	"(1) amounts received under workers' com-
20	pensation acts as compensation for personal injuries
21	or sickness;
22	"(2) the amount of any damages received
23	(whether by suit or agreement and whether as lump
24	sums or as periodic payments) on account of per-
25	sonal injuries or sickness;

- 1 "(3) amounts received through accident or 2 health insurance for medical care;
- "(4) amounts received through accident or health insurance for personal injuries or sickness (other than for medical care), but only to the extent such amounts (A) are not attributable to contributions by the employer which were not includible in the gross income of the employee, and are (B) not are paid by the employer;
 - "(5) amounts received as pension, annuity, or similar allowance for personal injuries or sickness resulting from active service in the armed forces of any country or in the Coast and Geodetic Survey or the Public Health Service, or as a disability annuity payable under the provisions of section 808 of the Foreign Service Act of 1980; and
 - "(6) amounts received by an individual as disability income attributable to injuries incurred as a direct result of a violent attack which the Secretary of State determines to be a terrorist attack and which occurred while such individual was an employee of the United States engaged in the performance of his official duties outside the United States.

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1	Paragraph (2) shall not apply to any punitive dam-
2	ages in connection with a case not involving physical
3	injury or physical sickness.
4	"(b) Termination of Application of Subsection
5	(a)(4) IN CERTAIN CASES.—
6	"(1) In general.—Subsection (a)(4) shall not
7	apply in the case of an individual who is not de-
8	scribed in paragraph (2).
9	"(2) Individuals to whom subsection
10	(a)(4) Continues to apply.—An individual is de-
11	scribed in this paragraph if—
12	"(A) on or before September 24, 1975, he
13	was entitled to receive any amount described in
14	subsection (a)(4),
15	"(B) on September 24, 1975, he was a
16	member of any organization (or reserve compo-
17	nent thereof) referred to in subsection (a)(4) or
18	under a binding written commitment to become
19	such a member,
20	"(C) he receives an amount described in
21	subsection (a)(4) by reason of a combat-related
22	injury, or
23	"(D) on application therefore, he would be
24	entitled to receive disability compensation from
25	the Veterons' Administration

1	"(3) Special rules for combat-related in-
2	JURIES.—For purposes of this subsection, the term
3	'combat-related injury' means personal injury or
4	sickness—
5	"(A) which is incurred—
6	"(i) as a direct result of armed con-
7	flict,
8	"(ii) while engaged in extrahazardous
9	service, or
10	"(iii) under conditions simulating war;
11	or
12	"(B) which is caused by an instrumentality
13	of war.
14	In the case of an individual who is not described in
15	subparagraph (A) or (B) of paragraph (2), except as
16	provided in paragraph (4), the only amounts taken
17	into account under subsection (a)(4) shall be the
18	amounts which he receives by reason of a combat-
19	related injury.
20	"(4) Amount excluded to be not less
21	THAN VETERANS' DISABILITY COMPENSATION.—In
22	the case of any individual described in paragraph
23	(2), the amounts excludable under subsection (a)(4)
24	for any period with respect to any individual shall
25	not be less than the maximum amount which such

1	individual, on application therefor, would be entitled
2	to receive as disability compensation from the Veter-
3	ans' Administration.
4	"SEC. 96. MEALS OR LODGING FURNISHED FOR THE CON-
5	VENIENCE OF THE EMPLOYER.
6	"(a) Meals and Lodging Furnished to Em-
7	PLOYEE, HIS SPOUSE, AND HIS DEPENDENTS, PURSU-
8	ANT TO EMPLOYMENT.—There shall be excluded from
9	gross income of an employee the value of any meals or
10	lodging furnished to him, his spouse, or any of his depend-
11	ents by or on behalf of his employer for the convenience
12	of the employer, but only if—
13	"(1) in the case of meals, the meals are fur-
14	nished on the business premises of the employer, or
15	"(2) in the case of lodging, the employee is re-
16	quired to accept such lodging on the business prem-
17	ises of his employer as a condition of his employ-
18	ment.
19	"(b) Special Rules.—For the purposes of sub-
20	section (a)—
21	"(1) Provisions of employment contract
22	OR STATE STATUTE NOT TO BE DETERMINATIVE.—
23	In determining whether meals or lodging are fur-
24	nished for the convenience of the employer, the pro-
25	visions of an employment contract or of a State stat-

1	ute fixing terms of employment shall not be deter-
2	minative of whether the meals or lodging are in-
3	tended as compensation.
4	"(2) Certain factors not taken into ac-
5	COUNT WITH RESPECT TO MEALS.—In determining
6	whether meals are furnished for the convenience of
7	the employer, the fact that a charge is made for
8	such meals, and the fact that the employee may ac-
9	cept or decline such meals, shall not be taken into
10	account.
11	"(3) CERTAIN FIXED CHARGES FOR MEALS.—
12	"(A) In general.—If—
13	"(i) an employee is required to pay on
14	a periodic basis a fixed charge for his
15	meals, and
16	"(ii) such meals are furnished by the
17	employer for the convenience of the em-
18	ployer,
19	there shall be excluded from the employee's
20	gross income an amount equal to such fixed
21	charge.
22	"(B) APPLICATION OF SUBPARAGRAPH
23	(A).—Subparagraph (A) shall apply—

1	"(i) whether the employee pays the fixed charge
2	out of his stated compensation or out of his own
3	funds, and
4	"(ii) only if the employee is required to make
5	the payment whether he accepts or declines the
6	meals.
7	"(c) Employees Living in Certain Camps.—
8	"(1) In general.—In the case of an individual
9	who is furnished lodging in a camp located in a for-
10	eign country by or on behalf of his employer, such
11	camp shall be considered to be part of the business
12	premises of the employer.
13	"(2) Camp.—For purposes of this section, a
14	camp constitutes lodging which is—
15	"(A) provided by or on behalf of the em-
16	ployer for the convenience of the employer be-
17	cause the place at which such individual renders
18	services is in a remote area where satisfactory
19	housing is not available on the open market,
20	"(B) located, as near as practicable, in the
21	vicinity of the place at which such individual
22	renders services, and
23	"(C) furnished in a common area (or en-
24	clave) which is not available to the public and

1	which normally accommodates 10 or more em-
2	ployees.
3	"(d) Lodging Furnished by Certain Edu-
4	CATIONAL INSTITUTIONS TO EMPLOYEES.—
5	"(1) IN GENERAL.—In the case of an employee
6	of an educational institution, gross income shall not
7	include the value of qualified campus lodging fur-
8	nished to such employee during the taxable year.
9	"(2) Exception in cases of inadequate
10	RENT.—Paragraph (1) shall not apply to the extent
11	of the excess of—
12	"(A) the lesser of—
13	"(i) 5 percent of the appraised value
14	of the qualified campus lodging, or
15	"(ii) the average of the rentals paid
16	by individuals (other than employees or
17	students of the educational institution)
18	during such calendar year for lodging pro-
19	vided by the educational institution which
20	is comparable to the qualified campus lodg-
21	ing provided to the employee, over
22	"(B) the rent paid by the employee for the
23	qualified campus lodging during such calendar
24	year.

1	The appraised value under subparagraph (A)(i) shall
2	be determined as of the close of the calendar year
3	in which the taxable year begins, or, in the case of
4	a rental period not greater than 1 year, at any time
5	during the calendar year in which such period be-
6	gins.
7	"(3) Qualified campus lodging.—For pur-
8	poses of this subsection, the term 'qualified campus
9	lodging' means lodging to which subsection (a) does
10	not apply and which is—
11	"(A) located on, or in the proximity of, a
12	campus of the educational institution, and
13	"(B) furnished to the employee, his spouse,
14	and any of his dependents by or on behalf of
15	such institution for use as a residence.
16	"(4) Educational institution.—For pur-
17	poses of this paragraph, the term 'educational insti-
18	tution' means an eligible educational institution as
19	defined in section $10(b)(2)(B)$.
20	"SEC. 97. CERTAIN FRINGE BENEFITS.
21	"(a) Purpose.—This section includes definitions and
22	rules applicable to the exclusion from gross income for cer-
23	tain fringe benefits.

1	"(b) No-Additional-Cost Service Defined.—
2	'No-additional-cost service' means any service provided by
3	an employer to an employee for use by such employee if—
4	"(1) such service is offered for sale to cus-
5	tomers in the ordinary course of the line of business
6	of the employer in which the employee is performing
7	services, and
8	"(2) the employer incurs no substantial addi-
9	tional cost (including forgone revenue) in providing
10	such service to the employee (determined without re-
11	gard to any amount paid by the employee for such
12	service).
13	"(c) Qualified Employee Discount Defined.—
14	"(1) QUALIFIED EMPLOYEE DISCOUNT.—The
15	term 'qualified employee discount' means any em-
16	ployee discount with respect to qualified property or
17	services to the extent such discount does not
18	exceed—
19	"(A) in the case of property, the gross
20	profit percentage of the price at which the prop-
21	erty is being offered by the employer to cus-
22	tomers, or
23	"(B) in the case of services, 20 percent of
24	the price at which the services are being offered
25	by the employer to customers.

1	"(2) Gross profit percentage.—
2	"(A) In general.—"Gross profit percent-
3	age' means the percent which—
4	"(i) the excess of the aggregate sales
5	price of property sold by the employer to
6	customers over the aggregate cost of such
7	property to the employer, is of
8	"(ii) the aggregate sales price of such
9	property.
10	"(B) Determination of gross profit
11	PERCENTAGE.—Gross profit percentage shall be
12	determined on the basis of—
13	"(i) all property offered to customers
14	in the ordinary course of the line of busi-
15	ness of the employer in which the employee
16	is performing services (or a reasonable
17	classification of property selected by the
18	employer), and
19	"(ii) the employer's experience during a
20	representative period.
21	"(3) Employee discount defined.—'Em-
22	ployee discount' means the amount by which—
23	"(A) the price at which the property or
24	services are provided by the employer to an em-
25	plovee for use by such employee, is less than

1	"(B) the price at which such property or
2	services are being offered by the employer to
3	customers.
4	"(4) Qualified property or services.—
5	'Qualified property or services' means any property
6	(other than real property and other than personal
7	property of a kind held for investment) or services
8	which are offered for sale to customers in the ordi-
9	nary course of the line of business of the employer
10	in which the employee is performing services.
11	"(c) DE MINIMIS FRINGE DEFINED.—
12	"(1) In general.—'De minimis fringe' means
13	any property or service the value of which is (after
14	taking into account the frequency with which similar
15	fringes are provided by the employer to the employ-
16	er's employees) so small as to make accounting for
17	it unreasonable or administratively impracticable.
18	"(2) Treatment of certain eating facili-
19	TIES.—The operation by an employer of any eating
20	facility for employees shall be treated as a de mini-
21	mis fringe if—
22	"(A) such facility is located on or near the
23	business premises of the employer, and

1	"(B) revenue derived from such facility
2	normally equals or exceeds the direct operating
3	costs of such facility.
4	The preceding sentence shall apply with respect to
5	any highly compensated employee only if access to
6	the facility is available on substantially the same
7	terms to each member of a group of employees
8	which is defined under a reasonable classification set
9	up by the employer which does not discriminate in
10	favor of highly compensated employees.
11	"(3) On-premises gyms and other athletic
12	FACILITIES.—
13	"(A) In general.—De minimis fringe
14	benefits include the provision of on-premises
15	athletic facility by an employer to its employees.
16	"(B) On-premises athletic facility.—
17	For purposes of this paragraph, 'on-premises
18	athletic facility' means any gym or other ath-
19	letic facility—
20	"(i) which is located on the premises
21	of the employer,
22	"(ii) which is operated by the em-
23	ployer, and

1	"(iii) substantially all the use of which
2	is by employees of the employer, their
3	spouses, and their dependent children.
4	"(d) CERTAIN EDUCATIONAL TRAINING BENE-
5	FITS.—Amounts paid or expenses incurred by the em-
6	ployer for education or training provided to the employee
7	shall be excluded from gross income under section 4 if
8	(and only if) such amounts or expenses are ordinary and
9	necessary business expenses and are not for an advanced
10	degree or to qualify an employee for a new line of work
11	"(e) Regulations.—The Secretary shall prescribe
12	regulations under this section, including regulations that
13	continue certain rules contained in section 132 to the In-
14	ternal Revenue Code of 1986 related to the fringe benefits
15	described in this section.
16	"Subchapter E—Rules Relating to Deductions
	"Sec. 101. Charitable, etc. organizations. "Sec. 102. Private foundations.
17	"SEC. 101. CHARITABLE, ETC. ORGANIZATIONS.
18	"(a) Purpose.—This section provides definitions for
19	purposes of determining the philanthropic transfer deduc-
20	tion and for other purposes of this chapter and chapter
21	2.
22	"(b) Regular Charity.—

1	"(A) REGULAR CHARITY.—"Regular char-
2	ity' means—
3	"(i) a church or a convention or asso-
4	ciation of churches,
5	"(ii) an educational organization
6	which normally maintains a regular faculty
7	and curriculum and normally has a regu-
8	larly enrolled body of pupils or students in
9	attendance at the place where its edu-
10	cational activities are regularly carried on,
11	"(iii) an organization the principal
12	purpose or functions of which are the pro-
13	viding of medical or hospital care or medi-
14	cal education or medical research, if the
15	organization is a hospital, or if the organi-
16	zation is a medical research organization
17	directly engaged in the continuous active
18	conduct of medical research in conjunction
19	with a hospital,
20	"(iv) an organization which normally
21	receives a substantial part of its support
22	(exclusive of income received in the exer-
23	cise or performance by such organization
24	of its charitable, educational, or other pur-
25	pose or function constituting the basis for

1 its exemption under section 253(a)) from 2 the United States or any State or political subdivision thereof or from direct or indi-3 rect contributions from the general public, and which is organized and operated exclu-6 sively to receive, hold, invest, and admin-7 ister property and to make expenditures to 8 or for the benefit of a college or university 9 which is an organization referred to in 10 clause (ii) of this subparagraph and which 11 is an agency or instrumentality of a State 12 or political subdivision thereof, or which is 13 owned or operated by a State or political 14 subdivision thereof or by an agency or in-15 strumentality of one or more States or po-16 litical subdivisions, "(v) a governmental unit referred to 17 18 in subsection (c)(1), 19

"(vi) an organization referred to in subsection (c)(2) which normally receives a substantial part of its support (exclusive of income received in the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption

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1	under section 253(a)) from a governmental
2	unit referred to in subsection $(c)(1)$ or
3	from direct or indirect contributions from
4	the general public,
5	"(vii) a private foundation described
6	in subparagraph (C), or
7	"(viii) an organization described in
8	section 102(a) (2) or (3).
9	"(B) Special rule for medical re-
10	SEARCH ORGANIZATIONS.—For purposes of de-
11	termining whether a contribution is to a regular
12	charity, a medical research organization shall
13	not be treated as described in clause (iii) of
14	paragraph (2) unless during the calendar year
15	in which the contribution is made such organi-
16	zation is committed to spend such contributions
17	for such research before January 1 of the fifth
18	calendar year which begins after the date such
19	contribution is made,
20	"(C) CERTAIN PRIVATE FOUNDATIONS.—
21	The private foundations referred to in subpara-
22	graph $(A)(vii)$ and subsection $(e)(1)(B)$ are—
23	"(i) a private operating foundation (as
24	defined in section $4942(j)(3)$,

1	"(ii) any other private foundation (as
2	defined in section 102(a)) which, not later
3	than the 15th day of the third month after
4	the close of the foundation's taxable year
5	in which contributions are received, makes
6	qualifying distributions (as defined in sec-
7	tion 4942(g), without regard to paragraph
8	(3) thereof), which are treated, after the
9	application of section 4942(g)(3), as dis-
10	tributions out of corpus (in accordance
11	with section 4942(h)) in an amount equal
12	to 100 percent of such contributions, and
13	with respect to which the taxpayer obtains
14	adequate records or other sufficient evi-
15	dence from the foundation showing that
16	the foundation made such qualifying dis-
17	tributions, and
18	"(iii) a private foundation all of the
19	contributions to which are pooled in a com-
20	mon fund and which would be described in
21	section 102(a)(3) but for the right of any
22	substantial contributor (hereafter in this
23	clause called 'donor') or his spouse to des-
24	ignate annually the recipients, from among

organizations described in paragraph (1) of

1 section 102(a), of the income attributable 2 to the donor's contribution to the fund and 3 to direct (by deed or by will) the payment, to an organization described in such paragraph (1), of the corpus in the common 6 fund attributable to the donor's contribu-7 tion; but this clause shall apply only if all 8 of the income of the common fund is re-9 quired to be (and is) distributed to one or 10 more organizations described in such para-11 graph (1) not later than the 15th day of 12 the third month after the close of the tax-13 able year in which the income is realized 14 by the fund and only if all of the corpus 15 attributable to any donor's contribution to 16 the fund is required to be (and is) distrib-17 uted to one or more of such organizations 18 not later than one year after his death or 19 after the death of his surviving spouse if 20 she has the right to designate the recipi-21 ents of such corpus.

> "(2) References.—Any reference in other law or in legal documents to an organization described in a clause of section 170(b)(1)(A) of the Internal Revenue Code of 1986 shall constitute a reference to

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1	an organization described in the same clause of sec-
2	tion $101(b)(1)(A)$.
3	"(c) Charity.—For purposes of determining the de-
4	ductibility of a philanthropic transfer, 'charitable contribu-
5	tion' means a contribution or gift for the use of—
6	"(1) A State, a possession of the United States,
7	or any political subdivision of any of the foregoing,
8	or the United States or the District of Columbia,
9	but only if the contribution or gift is made for exclu-
10	sively public purposes.
11	"(2) A corporation, trust, or community chest,
12	fund, or foundation—
13	"(A) created or organized in the United
14	States or in any possession thereof, or under
15	the law of the United States, any State, the
16	District of Columbia, or any possession of the
17	United States;
18	"(B) organized and operated exclusively
19	for religious, charitable, scientific, literary, or
20	educational purposes (but only if no part of its
21	activities involve the provision of athletic facili-
22	ties or equipment) or for the prevention of cru-
23	elty to children or animals

1	"(C) no part of the net earnings of which
2	inures to the benefit of any private shareholder
3	or individual, and

"(D) which qualifies for exemption from the business tax under section 253(c) and is not disqualified for tax exemption by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

"(3) [intentionally deleted]

"(4) In the case of a contribution or gift by an individual, a domestic fraternal society, order, or association, operating under the lodge system, but only if such contribution or gift is to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals.

"(5) A cemetery company owned and operated exclusively for the benefit of its members, or any corporation chartered solely for burial purposes as a cemetery corporation and not permitted by its charter to engage in any business not necessarily incident to that purpose, if such company or corporation

1	is not operated for profit and no part of the net
2	earnings of such company or corporation inures to
3	the benefit of any private shareholder or individual.
4	"(d) Rules for Subsection (c).—
5	"(1) Limitations.—A contribution or gift by a
6	corporation to a trust, chest, fund, or foundation
7	shall be deductible by reason of subsection (c)(2)(B)
8	only if it is to be used within the United States or
9	any of its possessions exclusively for purposes speci-
10	fied in subparagraph (B).
11	"(2) References.—Any reference in other law
12	or in legal documents to an organization described
13	in a paragraph of section 170(c) of the Internal Rev-
14	enue Code of 1986 shall constitute a reference to an
15	organization described in the same paragraph num-
16	ber of section 101(c) if an organization is described
17	in such paragraph.
18	"(e) Qualified Conservation Contribution.—
19	"(1) In general.—'Qualified conservation con-
20	tribution' means a contribution—
21	"(A) of a qualified real property interest,
22	"(B) to a qualified organization,
23	"(C) exclusively for conservation purposes.

1	"(2) Qualified real property interest.—
2	'Qualified real property interest' means any of the
3	following interests in real property:
4	"(A) the entire interest of the donor other
5	than a qualified mineral interest,
6	"(B) a remainder interest, and
7	"(C) a restriction (granted in perpetuity)
8	on the use which may be made of the real prop-
9	erty.
10	"(3) Qualified organization.—For purposes
11	of paragraph (1), the term 'qualified organization'
12	means an organization which—
13	"(A) is described in clause (v) or (vi) of
14	subsection (b)(1)(A), or
15	"(B) is described in section 253(c)(3)
16	and—
17	"(i) meets the requirements of section
18	102(a)(2), or
19	"(ii) meets the requirements of sec-
20	tion 102(a)(3) and is controlled by an or-
21	ganization described in subparagraph (A)
22	or in clause (i) of this subparagraph.
23	"(4) Conservation purpose defined.—

1	"(A) In general.—For purposes of this
2	subsection, the term 'conservation purpose'
3	means—
4	"(i) the preservation of land areas for
5	outdoor recreation by, or the education of,
6	the general public,
7	"(ii) the protection of a relatively nat-
8	ural habitat of fish, wildlife, or plants, or
9	similar ecosystem,
10	"(iii) the preservation of open space
11	(including farmland and forest land) where
12	such preservation is—
13	"(I) for the scenic enjoyment of
14	the general public, or
15	"(II) pursuant to a clearly delin-
16	eated Federal, State, or local govern-
17	mental conservation policy, and will
18	yield a significant public benefit, or
19	"(iv) the preservation of an histori-
20	cally important land area or a certified his-
21	toric structure.
22	"(B) Certified Historic Structure.—
23	For purposes of subparagraph (A)(iv), the term
24	'certified historic structure' means any building,
25	structure, or land area which—

1	"(i) is listed in the National Register,
2	Ol°
3	"(ii) is located in a registered historic
4	district and is certified by the Secretary of
5	the Interior to the Secretary as being of
6	historic significance to the district.
7	A building, structure, or land area satisfies the
8	preceding sentence if it satisfies such sentence
9	either at the time of the transfer or on the due
10	date (including extensions) for filing the trans-
11	feror's return under this chapter for the taxable
12	year in which the transfer is made.
13	"(5) Exclusively for conservation pur-
14	Poses.—For purposes of this subsection—
15	"(A) Conservation purpose must be
16	PROTECTED.—A contribution shall not be treat-
17	ed as exclusively for conservation purposes un-
18	less the conservation purpose is protected in
19	perpetuity.
20	"(B) No surface mining permitted.—
21	"(i) In general.—Except as pro-
22	vided in clause (ii), in the case of a con-
23	tribution of any interest where there is a
24	retention of a qualified mineral interest,
25	subparagraph (A) shall not be treated as

1	met if at any time there may be extraction
2	or removal of minerals by any surface min-
3	ing method.
4	"(ii) Special rule.—With respect to
5	any contribution of property in which the
6	ownership of the surface estate and min-
7	eral interests were separated before June
8	13, 1976, and remain so separated, sub-
9	paragraph (A) shall be treated as met if
10	the probability of surface mining occurring
11	on such property is so remote as to be neg-
12	ligible.
13	"(6) Qualified mineral interest.—For
14	purposes of this subsection, the term 'qualified min-
15	eral interest' means—
16	"(A) subsurface oil, gas, or other minerals,
17	and
18	"(B) the right to access to such minerals.
19	"(f) Denial of Deduction for Certain Travel
20	Expenses.—No deduction shall be allowed under section
21	211 for traveling expenses (including amounts expended
22	for meals and lodging) while away from home, whether
23	paid directly or by reimbursement, unless there is no sig-
24	nificant element of personal pleasure, recreation, or vaca-
25	tion in such travel.

- 1 "(g) Treatment of Certain Amounts Paid to or
- 2 For the Benefit of Institutions of Higher Edu-
- 3 CATION.—For purposes of section 11, if as the result of
- 4 a contribution to or for the benefit of an educational
- 5 organization—
- 6 "(1) which is described in subsection
- 7 (b)(1)(A)(ii), and
- 8 "(2) which is an institution of higher education
- 9 (as defined in section 3304(f))
- 10 the taxpayer receives (directly or indirectly) as a result
- 11 of paying such amount the right to purchase tickets for
- 12 seating at an athletic event in an athletic stadium of such
- 13 institution, 80 percent of such contribution shall be treat-
- 14 ed as a charitable contribution (but only if such amount
- 15 would be allowable as a deduction but for the fact that
- 16 the taxpayer received the right to purchase tickets). If any
- 17 portion of a payment is for the purchase of such tickets,
- 18 such portion and the remaining portion (if any) of such
- 19 payment shall be treated as separate amounts for purposes
- 20 of this subsection.

21 "Subchapter F—Special Business Activities

"Sec. 111. Rules of rental of real estate.

- 22 "SEC. 111. RULES FOR RENTAL OF REAL ESTATE.
- 23 "(a) IN GENERAL.—Except as provided in subsection
- 24 (b)—

1	"(1) the activity of rental of real estate is a
2	business activity to which the Simplified USA Tax
3	for businesses under chapter 2 applies,

- "(2) a taxpayer shall not be entitled to any deductions under this chapter with respect to rental property, and
- "(3) a taxpayer shall recognize gross income only with respect to distributions from the rental activity.

10 "(b) Insubstantial Rental Activity.—

- "(1) Not rental property.—If an individual or individuals own property, such individual or individuals and their families use the property on more than 14 days during the taxable year for nonbusiness purposes, the property is rented for no more than 14 days during the taxable year, and the total rental received by the individuals with respect to such property does not exceed \$10,000, the property shall not be considered rental property or used in the activity of rental of real estate during the taxable year for purposes of subsection (a) and the Simplified USA Tax for businesses under chapter 2.
- "(2) Rents from nonrental property.—

 Any rent from property described in paragraph (1)

1	shall be included in gross income for purposes of the
2	Simplified USA Income Tax.
3	"(c) Use for a Nonbusiness Purpose.—For pur-
4	poses of this section, 'use for a nonbusiness purpose'
5	means use other than—
6	"(1) use for which fair rent is paid,
7	"(2) use in connection with the preparation of
8	the property for rental, or
9	"(3) use that serves a clear business purpose.
10	Use during any part of a day shall constitute use for that
11	day.
12	"Subchapter G—Accounting Methods and
13	Periods
	"Sec. 121. Taxable year. "Sec. 122. Cash method of accounting; installment sales.
14	"SEC. 121. TAXABLE YEAR.
1415	"SEC. 121. TAXABLE YEAR. "(a) IN GENERAL.—The taxable year for all individ-
15 16	"(a) In General.—The taxable year for all individ-
15 16	"(a) In General.—The taxable year for all individ- uals subject to tax under this chapter shall be the calendar
15 16 17	"(a) In General.—The taxable year for all individ- uals subject to tax under this chapter shall be the calendar year except as provided in subsection (b).
15 16 17 18	"(a) IN GENERAL.—The taxable year for all individuals subject to tax under this chapter shall be the calendar year except as provided in subsection (b). "(b) Short Taxable Years.—
15 16 17 18 19	"(a) In General.—The taxable year for all individuals subject to tax under this chapter shall be the calendar year except as provided in subsection (b). "(b) Short Taxable Years.— "(1) Birth.—An individual's taxable year in
15 16 17 18 19 20	"(a) In General.—The taxable year for all individuals subject to tax under this chapter shall be the calendar year except as provided in subsection (b). "(b) Short Taxable Years.— "(1) Birth.—An individual's taxable year in year of his birth shall begin on the date of his birth.

1	"SEC. 122. CASH METHOD OF ACCOUNTING; INSTALLMENT
2	SALES.
3	"(a) In General.—All individuals shall determine
4	their income and deductions using the cash receipts and
5	disbursement method.
6	"(b) OID Rules.—
7	"(1) In general.—Original issue discount
8	shall not be included in gross income until received.
9	"(2) Previously recognized oid.—Original
10	issue discount included in income under the Internal
11	Revenue Code of 1986 shall increase the adjusted
12	basis of the instrument to which the original issue
13	discount related and shall not again be included in
14	income when received.
15	"(c) Installment Sales.—
16	"(1) In general.—Taxpayers shall take into
17	account income from installment sales when re-
18	ceived.
19	"(2) REGULATIONS.—The Secretary shall pro-
20	mulgate regulations implementing paragraph (1).
21	Such regulations shall generally follow the principles
22	of sections 453, 453A and 453B of the Internal Rev-
23	enue Code of 1986, except to the extent such prin-
24	ciples are inconsistent with other provisions of this
25	chapter.

1	"(d) Constructive Receipt.—Income shall be
2	treated as received when constructively received.
3	"(e) Effect of Change of Accounting Meth-
4	od.—Rules similar to those under section 226 shall apply
5	to ensure that a taxpayer does not deduct the same ex-
6	pense twice or include the same item in income twice.
7	"Subchapter H—Nonresident Aliens
	"Sec. 131. Tax on nonresident alien individuals. "Sec. 132. Tax treatment of certain community income of nonresident aliens.
8	"SEC. 131. TAX ON NONRESIDENT ALIEN INDIVIDUALS.
9	"(a) Nonbusiness Income.—
10	"(1) Income other than certain gains.—
11	There is hereby imposed for each taxable year a tax
12	of 30 percent of the amount received from sources
13	within the United States by a nonresident alien indi-
14	vidual as—
15	"(A) interest (other than portfolio interest
16	(as defined in subsection (b)(2)), deposit inter-
17	est (as defined in subsection (b)(3)) and origi-
18	nal issue discount, dividends, rents, salaries,
19	wages, premiums, annuities, compensations, re-
20	munerations, emoluments, and other fixed or
21	determinable annual periodical gains, profits
22	and income,

1	"(B) gains from the disposal of timber
2	coal, or iron ore with a retained economic inter-
3	est,
4	"(C) in the case of the sale of an original
5	discount obligation or payment on an original
6	issue discount obligation, the interest accrued
7	while the individual was a nonresident alien
8	and
9	"(D) includible social security benefits (as
10	defined in section $3(b)(2)$.
11	"(2) Capital gains of certain aliens.—In
12	the case of a nonresident alien individual present in
13	the United States for a period or periods aggregate
14	ing 183 days or more during the taxable year, there
15	is hereby imposed a tax of 30 percent of the amount
16	by which the gains, derived from sources within the
17	United States, from the sale or exchange at any
18	time during such year exceeds his losses, allocable
19	to sources within the United States, from the sale
20	or exchange at any time during such year of capital
21	assets.
22	"(3) Tax does not apply to business in-
23	COME.—The taxes imposed by this section shall not

apply to the income of any business entity, except to

1	the extent such income is distributed as compensa-
2	tion, dividends, or interest.
3	"(b) Special Rules and Definitions.—
4	"(1) Certain annuities.—The taxes imposed
5	by subsection (a) shall not apply to any amount re-
6	ceived as an annuity under a qualified annuity plan
7	described in section 403(a)(1), or from a qualified
8	trust described in section 401(a) and exempt under
9	section 253(a) if—
10	"(A) all of the personal services by reason
11	of which the annuity is payable were either—
12	"(i) personal services performed out-
13	side the United States by an individual
14	who, at the time of performance of such
15	personal services, was a nonresident alien,
16	or
17	"(ii) personal services by a non-
18	resident alien temporarily present in the
19	United States for a period or periods not
20	exceeding 90 days during a taxable year,
21	whose compensation for such services did
22	not exceed \$3,000, and who performed
23	such services for—
24	"(I) a nonresident alien individ-
25	ual, foreign partnership, or foreign

1	corporation, not engaged in a trade or
2	business within the United States, or
3	"(II) for an office or place of
4	business maintained in a foreign coun-
5	try or in a possession of the United
6	States by an individual who is a citi-
7	zen or resident of the United States
8	or by a domestic partnership or a do-
9	mestic corporation, and
10	"(B) at the time the first amount is paid
11	as annuity under the annuity plan or by the
12	trust, 90 percent or more of the employees for
13	whom contributions or benefits are provided
14	under such plan are citizens or residents of the
15	United States.
16	"(2) Portfolio interest.—
17	"(A) In General.—"Portfolio interest"
18	means—
19	"(i) interest on obligations in reg-
20	istered form if the United States person
21	who would otherwise be required to with-
22	hold tax on such interest under section
23	1441(a) receives a statement that the ben-
24	eficial owner of the obligation is not a
25	United States person, and

1	"(ii) interest on obligations in nonreg-
2	istered form if appropriate precautions are
3	taken to ensure that such obligations will
4	be sold only to persons who are not United
5	States persons and such interest is paid
6	outside the United States.
7	"(B) Exceptions.—Under rules to be
8	prescribed by the Secretary, portfolio interest
9	does not include—
10	"(i) interest received by a 10-percent
11	equity owner, or
12	"(ii) contingent interest.
13	"(3) Deposit interest".—"Deposit interest"
14	means interest on deposits which are—
15	"(A) deposits with persons carrying on a
16	banking business (including savings and loans),
17	and
18	"(B) amounts held by an insurance com-
19	pany under an agreement to pay interest there-
20	on.
21	"(4) Other exceptions.—The taxes imposed
22	by subsection (a) shall not apply to—
23	"(A) a percentage of any dividend paid by
24	a business entity, 80 percent of whose gross re-
25	ceipts are not taken into account under chapter

1	1 because they are from outside the United
2	States, equal to the percentage of gross receipts
3	not so taken into account,
4	"(B) gambling winnings (except to the ex-
5	tent that the Secretary determines by regula-
6	tion that the collection of the tax is administra-
7	tively feasible),
8	"(C) compensation paid by a foreign em-
9	ployer to a nonresident alien individual for the
10	period he is temporarily present in the United
11	States as a nonimmigrant under subparagraph
12	(F) or (J) of section 101(a)(15) of the Immi-
13	gration and Nationality Act, as amended,
14	"(D) interest from a series E or series H
15	savings bond if the individual acquired the bond
16	while a resident of the Ryuku Islands or the
17	Trust Territory of the Pacific Islands, or
18	"(E) amounts earned or payable to any
19	person who is a bona fide resident of Puerto
20	Rico, Guam, American Samoa, or the Northern
21	Mariana Islands (and, therefore, is subject to
22	the tax imposed by subchapter A).
23	"(c) Expatriation To Avoid Tax.—
24	"(1) IN GENERAL.—A nonresident alien individ-
25	ual who at any time within the 10-year period imme-

1	diately preceding the close of the taxable year lost
2	United States citizenship shall be taxable in the
3	manner described in paragraph (2) unless none of
4	the principal purposes of losing citizenship was
5	avoidance of tax under subchapter A or subtitle B
6	"(2) Alternative Tax.—A nonresident alien
7	individual described in paragraph (1) shall be sub-
8	ject to tax on the items taxable under subsection (a)
9	as determined without regard to exceptions listed or
10	based on definitions contained in subsection (b)
11	using the rate schedule for single individuals under
12	section 215. If the taxes determined under sub-
13	section (a) are greater than the tax determined
14	under this subsection, the greater tax shall apply.
15	"SEC. 132. TAX TREATMENT OF CERTAIN COMMUNITY IN
16	COME OF NONRESIDENT ALIENS.
17	"(a) General Rule.—In the case of a married cou-
18	ple one or both of whom are nonresident alien individuals
19	and who have community income for the taxable year
20	such community income shall be treated as follows:
21	"(1) Compensation income shall be treated as
22	income of the spouse who rendered the services,
23	"(2) Partnership distributions shall be treated
24	as the related distributive shares of partnership in-
25	come would be treated under section 1402(a)(5),

1	"(3) Community income which is derived from
2	the separate property of a spouse shall be treated as
3	income of that spouse, and
4	"(4) All other such community income shall be
5	treated as provided in the applicable community
6	property law.
7	"(b) Exception Where Election Under Sec-
8	TION 6013(g) IS IN EFFECT.—Subsection (a) shall not
9	apply if an election under subsection (g) or (h) of section
10	6013 (relating to election to treat nonresident alien indi-
11	viduals as residents of the United States) is in effect.
12	"SEC. 133. RELATIONSHIP WITH TREATIES.
13	"(a) Statement of Policy.—It is the intention of
14	the USA Tax Code to promote a worldwide tax system
15	in which each nation taxes—
16	"(1) under an individual tax, only the income of
17	individuals who are residents or citizens of that na-
18	tion, and
19	"(2) under a business tax only the business ac-
20	tivity in such nation.
21	"(b) Effect of Treaties.—No tax shall be im-
22	posed under section 131(a) on income that is exempt from
23	tax by reason of a treaty between the nation of which the
24	nonresident alien is a citizen or resident and the United

25 States. If any such treaty requires that a lower rate of

- 1 tax be imposed on some or all of the items of income sub-
- 2 ject to tax under section 331(a), such lower rate shall
- 3 apply to such items in the case of persons to whom such
- 4 treaty applies.
- 5 "(c) Effect of Unilateral Action by Foreign
- 6 Nation.—No tax shall be imposed under section 331(a)
- 7 on nonresident aliens who are citizens or residents of an-
- 8 other nation if—
- 9 "(1) such nation exempts from its income and
- 10 withholding taxes nonresident alien individuals who
- are residents or citizens of the United States,
- "(2) such nation has entered into a tax infor-
- mation sharing agreement with the United States,
- 14 and
- 15 "(3) the Secretary certifies that the preceding
- two requirements have been satisfied.

17 "Subchapter I—Trusts and Estates

- "Sec. 140. Prepayment of tax by trusts and estates.
- "Sec. 141. Application of tax.
- "Sec. 142. Special rules for credits and deductions.
- "Sec. 143. Definitions and rules applicable to subchapter I.
- "Sec. 144. Deduction for trusts distributing current income only.
- "Sec. 145. Inclusion of amounts in gross income of beneficiaries of trusts distributing current income only.
- "Sec. 146. Deduction for estates and trusts accumulating income or distributing corpus.
- "Sec. 147. Inclusion of amounts in gross income of beneficiaries of estates and trusts accumulating income or distributing corpus.
- "Sec. 148. Special rules applicable to sections 146 and 147.
- "Sec. 149. Charitable remainder trusts.
- "Sec. 150. Definitions applicable to excess distribution rules.
- "Sec. 151. Accumulation distribution allocated to preceding years.
- "Sec. 152. Treatment of amounts deemed distributed by trust in preceding years.

200 "Sec. 153. Trust income, deductions, and credits attributable to grantors and others as substantial owners. "Sec. 154. Definitions and rules. "Sec. 155. Reversionary interests. "Sec. 156. Power to control beneficial enjoyment. "Sec. 157. Administrative powers. "Sec. 158. Power to revoke. "Sec. 159. Income for benefit of grantor. "Sec. 160. Person other than grantor treated as substantial owner. "Sec. 161. Foreign trusts having one or more United States beneficiaries. "Sec. 162. Limitation on charitable deduction. "Sec. 163. Income of an estate or trust in case of divorce, etc. "Sec. 164. Recognition of gain on certain transfers to certain foreign persons and estates. "Sec. 165. Treatment of funeral trusts. "Sec. 166. Income in respect of a decedent. "SEC. 140. PREPAYMENT OF TAX BY TRUSTS AND ESTATES. "(a) Prepayment of Tax.—A trust or estate shall prepay the Simplified USA Tax for individuals in accordance with the provisions of this subchapter. "(b) Imposition of Tax.—There is hereby imposed a tax on the taxable income of trusts and estates (as determined in accordance with this subchapter) a tax determined as follows: "If taxable income is: The tax is: Not over \$1,600 15% of taxable income. Over \$1,600, but not over \$3,800 \$240, plus 25% of the excess over \$1,600. Over \$3,800 \$790, plus 30% of the excess over \$3,800. "(c) Inflation Adjustment.—The schedule in subsection (b) shall be adjusted for inflation in accordance with section 23. "(d) Business Activities.—

"(1) Tax on business activity determined

AT BUSINESS LEVEL.—If a trust engages in business

activity (as defined in section 206(b)), it shall be

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1	considered a business entity with respect to such ac-
2	tivities for purposes of the business tax under chap-
3	ter 2. The business entity shall be considered an
4	asset of the trust.
5	"(2) Business entity as sole bene-
6	FICIARY.—If the only beneficiaries of a trust are
7	business entities, no tax shall be imposed on such
8	trust under this subchapter.
9	"SEC. 141. APPLICATION OF TAX.
10	"(a) In General.—The tax imposed by section 140
11	shall apply to the taxable income of estates or of any kind
12	of property held in trust, including—
13	"(1) income accumulated in trust for the bene-
14	fit of unborn or unascertained persons or persons
15	with contingent interests, and income accumulated
16	or held for future distribution under the terms of
17	the will or trust;
18	"(2) income which is to be distributed currently
19	by the fiduciary to the beneficiaries, and income col-
20	lected by a guardian of an infant which is to be held
21	or distributed as the court may direct;
22	"(3) income received by estates of deceased per-
23	sons during the period of administration or settle-

ment of the estate; and

1

"(4) income which, in the discretion of the fidu-

2	ciary, may be either distributed to the beneficiaries
3	or accumulated.
4	"(b) Computation and Payment.—The taxable in-
5	come of an estate or trust shall be computed in the same
6	manner as in the case of an individual, except as otherwise
7	provided in this subchapter. The tax shall be computed
8	on such taxable income and shall be paid by the fiduciary.
9	For purposes of this subsection, a foreign trust or foreign
10	estate shall be treated as a nonresident alien individual
11	who is not present in the United States at any time.
12	"(c) Exclusion of Includible Gain From Tax-
13	ABLE INCOME.—The taxable income of a trust does not
14	include the amount of any includible gain as defined in
15	section 144(b) reduced by any deductions properly alloca-
16	ble thereto.
17	"SEC. 142. SPECIAL RULES FOR CREDITS AND DEDUCTIONS.
18	"(a) USA DEDUCTION AND FAMILY LIVING ALLOW-
19	ANCE.—
20	"(1) No deduction or allowance.—A trust
21	or estate shall not be allowed any USA Deductions
22	or a Family Living Allowance.
23	"(2) Special deduction.—For purposes of
24	determining taxable income, trusts and estates shall

1	be entitled to the following deductions from gross
2	income—
3	"(A) Estate.—An estate shall be allowed
4	a deduction of \$600.
5	"(B) DISTRIBUTING TRUST.—A trust
6	which, under its governing instrument, is re-
7	quired to distribute all of its income currently
8	shall be allowed a deduction of \$300.
9	"(C) Other trusts.—Trusts not de-
10	scribed in subparagraph (B) shall be allowed a
11	deduction of \$100.
12	"(b) Deduction for Amounts Paid or Perma-
13	NENTLY SET ASIDE FOR A CHARITABLE PURPOSE.—
14	"(1) GENERAL RULE.—In the case of an estate
15	or trust, there shall be allowed as a deduction in
16	computing its taxable income (in lieu of the philan-
17	thropic transfer deduction) any amount of the gross
18	income, without limitation, which pursuant to the
19	terms of the governing instrument is, during the
20	taxable year, paid for a purpose specified in section
21	101(c) (determined without regard to section
22	101(c)(2)(A)). If a charitable contribution is paid
23	after the close of such taxable year and on or before
24	the last day of the year following the close of such
25	taxable year, then the trustee or administrator may

elect to treat such contribution as paid during such taxable year. The election shall be made at such time and in such manner as the Secretary prescribes by regulations.

- "(2) POOLED INCOME FUNDS.—In the case of a pooled income fund (as defined in paragraph (3)), there shall also be allowed as a deduction in computing its taxable income any amount of the gross income attributable to gain from the sale of a capital asset held for more than 1 year, without limitation, which pursuant to the terms of the governing instrument is, during the taxable year, permanently set aside for a purpose specified in section 101(c).
- "(3) DEFINITION OF POOLED INCOME FUND.—
 For purposes of paragraph (2), a pooled income fund is a trust—

"(A) to which each donor transfers property, contributing an irrevocable remainder interest in such property to or for the use of an organization described in section 101(b)(1)(A) (other than in clauses (vii) or (viii)), and retaining an income interest for the life of one or more beneficiaries (living at the time of such transfer),

1	"(B) in which the property transferred by
2	each donor is commingled with property trans-
3	ferred by other donors who have made or make
4	similar transfers,
5	"(C) which cannot have investments in se-
6	curities which are exempt from taxes imposed
7	by this subtitle,
8	"(D) which includes only amounts received
9	from transfers which meet the requirements of
10	this paragraph,
11	"(E) which is maintained by the organiza-
12	tion to which the remainder interest is contrib-
13	uted and of which no donor or beneficiary of an
14	income interest is a trustee, and
15	"(F) from which each beneficiary of an in-
16	come interest receives income, for each year for
17	which he is entitled to receive the income inter-
18	est referred to in subparagraph (A), determined
19	by the rate of return earned by the trust for
20	such year.
21	For purposes of determining the amount of any
22	charitable contribution allowable by reason of a
23	transfer of property to a pooled fund, the value of
24	the income interest shall be determined on the basis
25	of the highest rate of return earned by the fund for

- 1 any of the 3 taxable years immediately preceding the
- 2 taxable year of the fund in which the transfer is
- 3 made. In the case of funds in existence less than 3
- 4 taxable years preceding the taxable year of the fund
- 5 in which a transfer is made the rate of return shall
- 6 be deemed to be 6 percent per annum, except that
- 7 the Secretary may prescribe a different rate of re-
- 8 turn.
- 9 "(c) Unused Loss Carryovers.—If on the termi-
- 10 nation of an estate or trust, the estate or trust has a loss
- 11 carryover then such carryover shall be allowed as a deduc-
- 12 tion, in accordance with regulations prescribed by the Sec-
- 13 retary, to the beneficiaries succeeding to the property of
- 14 the estate or trust.
- 15 "(d) Certain Distributions by Cemetery Per-
- 16 PETUAL CARE FUNDS.—In the case of a cemetery perpet-
- 17 ual care fund which—
- 18 "(1) was created pursuant to local law by a tax-
- able cemetery corporation for the care and mainte-
- 20 nance of cemetery property, and
- 21 "(2) is treated for the taxable year as a trust
- for purposes of this subchapter,
- 23 any amount distributed by such fund for the care and
- 24 maintenance of gravesites which have been purchased
- 25 from the cemetery corporation before the beginning of the

1	taxable year of the trust and with respect to which there
2	is an obligation to furnish care and maintenance shall be
3	considered to be a distribution solely for purposes of sec-
4	tions 144 and 146, but only to the extent that the aggre-
5	gate amount so distributed during the taxable year does
6	not exceed \$5 multiplied by the aggregate number of such
7	gravesites.
8	"SEC. 143. DEFINITIONS AND RULES APPLICABLE TO SUB-
9	CHAPTER I.
10	For purposes of this subchapter—
11	"(a) DISTRIBUTABLE NET INCOME.—'Distributable
12	net income' means, with respect to any taxable year, the
13	taxable income of the estate or trust computed with the
14	following modifications—
15	"(1) No deduction shall be taken under sections
16	144 and 146 (relating to additional deductions).
17	"(2) No deduction shall be taken under section
18	142(a)(2) (relating to deduction for personal exemp-
19	tions).
20	"(3) Gains from the sale or exchange of capital
21	assets shall be excluded to the extent that such gains
22	are allocated to corpus and are not (A) paid, cred-
23	ited, or required to be distributed to any beneficiary
24	during the taxable year, or (B) paid, permanently
25	set aside, or to be used for the purposes specified

in section 142(b). Losses from the sale or exchange
of capital assets shall be excluded, except to the ex-
tent such losses are taken into account in determin-
ing the amount of gains from the sale or exchange
of capital assets which are paid, credited, or re-
quired to be distributed to any beneficiary during
the taxable year.

- "(4) For purposes only of rules under section _____, there shall be excluded those items of gross income constituting extraordinary dividends or taxable stock dividends which the fiduciary, acting in good faith, does not pay or credit to any beneficiary by reason of his determination that such dividends are allocable to corpus under the terms of the governing instrument and applicable local law.
- "(5) There shall be included any tax-exempt interest.

"(6) In the case of a foreign trust—

"(A) There shall be included the amounts of gross income from sources without the United States, reduced by any amounts which would be deductible in respect of disbursements allocable to such income but for the provisions of section 265(a)(1) (relating to disallowance of certain deductions).

1 "(B) Gross income from sources within the 2 United States shall be determined without re-3 gard to section 894 (relating to income exempt 4 under treaty).

"(C) Paragraph (3) shall not apply to a foreign trust. In the case of such a trust, there shall be included gains from the sale or exchange of capital assets, reduced by losses from such sales or exchanges to the extent such losses do not exceed gains from such sales or exchanges.

11 12 If the estate or trust is allowed a deduction under section 13 142(b), the amount of the modifications specified in paragraphs (5) and (6) shall be reduced to the extent that the 14 15 amount of income which is paid, permanently set aside, or to be used for the purposes specified in section 142(b) 16 is deemed to consist of items specified in those paragraphs. For this purpose, such amount shall (in the ab-18 19 sence of specific provisions in the governing instrument) 20 be deemed to consist of the same proportion of each class

"(b) Income.—'Income', when not preceded by the words 'taxable', 'distributable net', 'undistributed net', or 'gross', means the amount of income of the estate or trust

each class bears to the total of all classes.

of items of income of the estate or trust as the total of

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1	for the taxable year determined under the terms of the
2	governing instrument and applicable local law. Items of
3	gross income constituting extraordinary dividends or tax-
4	able stock dividends which the fiduciary, acting in good
5	faith, determines to be allocable to corpus under the terms
6	of the governing instrument and applicable local law shall
7	not be considered income.
8	"(c) Beneficiary.—'Beneficiary' includes heir, lega-
9	tee, devisee.
10	"(d) Treatment of Property Distributed in
11	Kind.—
12	"(1) Basis of Beneficiary.—The basis of any
13	property received by a beneficiary in a distribution
14	from an estate or trust shall be—
15	"(A) the adjusted basis of such property in
16	the hands of the estate or trust immediately be-
17	fore the distribution, adjusted for
18	"(B) any gain or loss recognized to the es-
19	tate or trust on the distribution.
20	"(2) Amount of distribution.—In the case
21	of any distribution of property (other than cash), the
22	amount taken into account under sections 146(a)(2)
23	and 147(a)(2) shall be the lesser of—

1	"(A) the basis of such property in the
2	hands of the beneficiary (as determined under
3	paragraph (1)), or
4	"(B) the fair market value of such prop-
5	erty.
6	"(3) Election to recognize gain.—
7	"(A) IN GENERAL.—In the case of any dis-
8	tribution of property (other than cash) to which
9	an election under this paragraph applies—
10	"(i) paragraph (2) shall not apply,
11	"(ii) gain or loss shall be recognized
12	by the estate or trust in the same manner
13	as if such property had been sold to the
14	distributee at its fair market value, and
15	"(iii) the amount taken into account
16	under sections $146(a)(2)$ and $147(a)(2)$
17	shall be the fair market value of such
18	property.
19	"(B) Election.—Any election under this
20	paragraph shall apply to all distributions made
21	by the estate or trust during a taxable year and
22	shall be made on the return of such estate or
23	trust for such taxable year.
24	Any such election, once made, may be revoked only
25	with the consent of the Secretary.

- 1 "(4) Exception for distributions de-
- 2 SCRIBED IN SECTION 148(a).—This subsection shall
- and apply to any distribution described in section
- 4 148(a).
- 5 "(f) Treatment of Multiple Trusts.—For pur-
- 6 poses of this subchapter, under regulations prescribed by
- 7 the Secretary, 2 or more trusts shall be treated as 1 trust
- 8 if—
- 9 "(1) such trusts have substantially the same
- grantor or grantors and substantially the same pri-
- 11 mary beneficiary or beneficiaries, and
- 12 "(2) a principal purpose of such trusts is the
- avoidance of the tax imposed by this chapter.
- 14 For purposes of the preceding sentence, a husband and
- 15 wife shall be treated as 1 person.
- 16 "(g) Certain Payments of Estimated Tax
- 17 Treated as Paid by Beneficiary.—Under rules pre-
- 18 scribed by the Secretary, a trustee may elect to treat any
- 19 portion of a payment of estimated tax made by such trust
- 20 for any taxable year of the trust as a payment made by
- 21 a beneficiary of such trust. This rule shall also apply in
- 22 the case of a taxable year reasonably expected to be the
- 23 last taxable year of an estate.
- 24 "(h) Foreign Trusts and Foreign Income.—The
- 25 Secretary shall prescribe special rules for foreign trusts

1	and foreign income of trusts. Those rules should generally
2	be consistent with the rules under subchapter J of chapter
3	1 of the Internal Revenue Code of 1986, except that they
4	shall take into account the principles of the Simplified
5	USA Tax.
6	"(i) CERTAIN REVOCABLE TRUSTS TREATED AS
7	PART OF ESTATE.
8	"(1) In general.—If both the executor (if
9	any) of an estate and the trustee of a qualified rev-
10	ocable trust elect the treatment provided in this sec-
11	tion, such trust shall be treated and taxed as part
12	of such estate (and not as a separate trust) for all
13	taxable years of the estate ending after the date of
14	the decedent's death and before the applicable date.
15	"(2) Qualified revocable trust.—For pur-
16	poses of this subsection, 'qualified revocable trust'
17	means any trust (or portion thereof) which was
18	treated under section 158 as owned by the decedent
19	of the estate referred to in paragraph (1) by reason
20	of a power in the grantor (determined without re-
21	gard to section 154(e).
22	"(3) Applicable date.—For purposes of this
23	subsection, 'applicable date' means—
24	"(A) if no return of tax imposed by chap-
25	ter 11 is required to be filed, the date which is

1	2 years after the date of the decedent's death,
2	and
3	"(B) if such a return is required to be
4	filed, the date which is 6 months after the date
5	of the final determination of the liability for tax
6	imposed by chapter 11.
7	"(4) Election.—The election under this sub-
8	section shall be made not later than the time pre-
9	scribed for filing the return of tax imposed by this
10	chapter for the first taxable year of the estate (de-
11	termined with regard to extensions) and, once made,
12	shall be irrevocable.
13	"SEC. 144. DEDUCTION FOR TRUSTS DISTRIBUTING CUR-
1314	"SEC. 144. DEDUCTION FOR TRUSTS DISTRIBUTING CUR- RENT INCOME ONLY.
14	RENT INCOME ONLY.
14 15	RENT INCOME ONLY. "(a) DEDUCTION.—In the case of any trust the terms
141516	RENT INCOME ONLY. "(a) DEDUCTION.—In the case of any trust the terms of which—
14 15 16 17	"(a) Deduction.—In the case of any trust the terms of which— "(1) provide that all of its income is required
14 15 16 17 18	"(a) Deduction.—In the case of any trust the terms of which— "(1) provide that all of its income is required to be distributed currently, and
141516171819	"(a) Deduction.—In the case of any trust the terms of which— "(1) provide that all of its income is required to be distributed currently, and "(2) do not provide that any amounts are to be
14 15 16 17 18 19 20	"(a) Deduction.—In the case of any trust the terms of which— "(1) provide that all of its income is required to be distributed currently, and "(2) do not provide that any amounts are to be paid, permanently set aside, or used for the purposes
14 15 16 17 18 19 20 21	"(a) Deduction.—In the case of any trust the terms of which— "(1) provide that all of its income is required to be distributed currently, and "(2) do not provide that any amounts are to be paid, permanently set aside, or used for the purposes specified in section 142(b) (relating to deduction for
14 15 16 17 18 19 20 21 22	"(a) Deduction.—In the case of any trust the terms of which— "(1) provide that all of its income is required to be distributed currently, and "(2) do not provide that any amounts are to be paid, permanently set aside, or used for the purposes specified in section 142(b) (relating to deduction for charitable, etc., purposes),

- 1 rently. This section shall not apply in any taxable year
- 2 in which the trust distributes amounts other than amounts
- 3 of income described in paragraph (1).
- 4 "(b) Limitation on Deduction.—If the amount of
- 5 income required to be distributed currently exceeds the
- 6 distributable net income of the trust for the taxable year,
- 7 the deduction shall be limited to the amount of the distrib-
- 8 utable net income. For this purpose, the computation of
- 9 distributable net income shall not include items of income
- 10 which are not included in the gross income of the trust
- 11 and the deductions allocable thereto.
- 12 "SEC. 145. INCLUSION OF AMOUNTS IN GROSS INCOME OF
- 13 BENEFICIARIES OF TRUSTS DISTRIBUTING
- 14 CURRENT INCOME ONLY.
- 15 "(a) INCLUSION.—Subject to subsection (b), the
- 16 amount of income for the taxable year required to be dis-
- 17 tributed currently by a trust described in section 144 shall
- 18 be included in the gross income of the beneficiaries to
- 19 whom the income is required to be distributed, whether
- 20 distributed or not. If such amount exceeds the distribut-
- 21 able net income, there shall be included in the gross in-
- 22 come of each beneficiary an amount which bears the same
- 23 ratio to distributable net income as the amount of income
- 24 required to be distributed to such beneficiary bears to the

- 1 amount of income required to be distributed to all bene-
- 2 ficiaries.
- 3 "(b) Character of Amounts.—The amounts speci-
- 4 fied in subsection (a) shall have the same character in the
- 5 hands of the beneficiary as in the hands of the trust. For
- 6 this purpose, the amounts shall be treated as consisting
- 7 of the same proportion of each class of items entering into
- 8 the computation of distributable net income of the trust
- 9 as the total of each class bears to the total distributable
- 10 net income of the trust, unless the terms of the trust spe-
- 11 cifically allocate different classes of income to different
- 12 beneficiaries. In the application of the preceding sentence,
- 13 the items of deduction entering into the computation of
- 14 distributable net income shall be allocated among the
- 15 items of distributable net income in accordance with regu-
- 16 lations prescribed by the Secretary.
- 17 "SEC. 146. DEDUCTION FOR ESTATES AND TRUSTS ACCU-
- 18 MULATING INCOME OR DISTRIBUTING
- 19 **CORPUS.**
- 20 "(a) Deduction.—In any taxable year there shall be
- 21 allowed as a deduction in computing the taxable income
- 22 of an estate or trust (other than a trust described in sec-
- 23 tion 144), the sum of—
- 24 "(1) any amount of income for such taxable
- year required to be distributed currently (including

- any amount required to be distributed which may be
- 2 paid out of income or corpus to the extent such
- amount is paid out of income for such taxable year);
- 4 and
- 5 "(2) any other amounts properly paid or cred-
- 6 ited or required to be distributed for such taxable
- 7 year;
- 8 but such deduction shall not exceed the distributable
- 9 net income of the estate or trust.
- 10 "(b) Character of Amounts Distributed.—The
- 11 amount determined under subsection (a) shall be treated
- 12 as consisting of the same proportion of each class of items
- 13 entering into the computation of distributable net income
- 14 of the estate or trust as the total of each class bears to
- 15 the total distributable net income of the estate or trust
- 16 in the absence of the allocation of different classes of in-
- 17 come under the specific terms of the governing instru-
- 18 ment. In the application of the preceding sentence, the
- 19 items of deduction entering into the computation of dis-
- 20 tributable net income (including the deduction allowed
- 21 under section 142(b)) shall be allocated among the items
- 22 of distributable net income in accordance with regulations
- 23 prescribed by the Secretary.
- 24 "(c) Limitation on Deduction.—No deduction
- 25 shall be allowed under subsection (a) in respect of any por-

- 1 tion of the amount allowed as a deduction under that sub-
- 2 section (without regard to this subsection) which is treated
- 3 under subsection (b) as consisting of any item of distribut-
- 4 able net income which is not included in the gross income
- 5 of the estate or trust.
- 6 "SEC. 147. INCLUSION OF AMOUNTS IN GROSS INCOME OF
- 7 BENEFICIARIES OF ESTATES AND TRUSTS AC-
- 8 CUMULATING INCOME OR DISTRIBUTING
- 9 **CORPUS.**
- 10 "(a) Inclusion.—Subject to subsection (b), there
- 11 shall be included in the gross income of a beneficiary to
- 12 whom an amount specified in section 146(a) is paid, cred-
- 13 ited, or required to be distributed (by an estate or trust
- 14 described in section 146), the sum of the following
- 15 amounts:
- 16 "(1) Amounts required to be distributed
- 17 CURRENTLY.—The amount of income for the taxable
- year required to be distributed currently to such
- beneficiary, whether distributed or not. If the
- amount of income required to be distributed cur-
- 21 rently to all beneficiaries exceeds the distributable
- 22 net income (computed without the deduction allowed
- by section 142(b), relating to deduction for chari-
- table, etc., purposes) of the estate or trust, then, in
- lieu of the amount provided in the preceding sen-

1	tence, there shall be included in the gross income of
2	the beneficiary an amount which bears the same
3	ratio to distributable net income (as so computed) as
4	the amount of income required to be distributed cur-
5	rently to such beneficiary bears to the amount re-
6	quired to be distributed currently to all beneficiaries.
7	For purposes of this section, the phrase 'the amount
8	of income for the taxable year required to be distrib-
9	uted currently' includes any amount required to be
10	paid out of income or corpus to the extent such
11	amount is paid out of income for such taxable year.
12	"(2) OTHER AMOUNTS DISTRIBUTED.—All
13	other amounts properly paid, credited, or required to
14	be distributed to such beneficiary for the taxable
15	year. If the sum of—
16	"(A) the amount of income for the taxable
17	year required to be distributed currently to all
18	beneficiaries, and
19	"(B) all other amounts properly paid, cred-
20	ited, or required to be distributed to all bene-
21	ficiaries
22	exceeds the distributable net income of the estate or
23	trust, then, in lieu of the amount provided in the
24	preceding sentence, there shall be included in the
25	gross income of the beneficiary an amount which

- 1 bears the same ratio to distributable net income (re-
- 2 duced by the amounts specified in (A)) as the other
- amounts properly paid, credited or required to be
- 4 distributed to the beneficiary bear to the other
- 5 amounts properly paid, credited, or required to be
- 6 distributed to all beneficiaries.
- 7 "(b) Character of Amounts.—The amounts de-
- 8 termined under subsection (a) shall have the same char-
- 9 acter in the hands of the beneficiary as in the hands of
- 10 the estate or trust. For this purpose, the amounts shall
- 11 be treated as consisting of the same proportion of each
- 12 class of items entering into the computation of distribut-
- 13 able net income as the total of each class bears to the
- 14 total distributable net income of the estate or trust unless
- 15 the terms of the governing instrument specifically allocate
- 16 different classes of income to different beneficiaries. In the
- 17 application of the preceding sentence, the items of deduc-
- 18 tion entering into the computation of distributable net in-
- 19 come (including the deduction allowed under section
- 20 142(b)) shall be allocated among the items of distributable
- 21 net income in accordance with regulations prescribed by
- 22 the Secretary. In the application of this subsection to the
- 23 amount determined under paragraph (1) of subsection (a),
- 24 distributable net income shall be computed without regard

1	to any portion of the deduction under section 142(b) which
2	is not attributable to income of the taxable year.
3	"SEC. 148. SPECIAL RULES APPLICABLE TO SECTIONS 146
4	AND 147.
5	"(a) Exclusions.—There shall not be included as
6	amounts falling within section 146(a) or 147(a)—
7	"(1) GIFTS, BEQUESTS, ETC.—Any amount
8	which, under the terms of the governing instrument,
9	is properly paid or credited as a gift or bequest of
10	a specific sum of money or of specific property and
11	which is paid or credited all at once or in not more
12	than 3 installments. For this purpose an amount
13	which can be paid or credited only from the income
14	of the estate or trust shall not be considered as a
15	gift or bequest of a specific sum of money.
16	"(2) Charitable, etc., distributions.—Any
17	amount paid or permanently set aside or otherwise
18	qualifying for the deduction provided in section
19	142(b) (computed without regard to sections 508(d),
20	162, and $4948(c)(4)$).
21	"(3) Denial of double deduction.—Any
22	amount paid, credited, or distributed in the taxable
23	year, if section 144 or section 146 applied to such

amount for a preceding taxable year of an estate or

- 1 trust because credited or required to be distributed
- 2 in such preceding taxable year.
- 3 "(b) Distributions in First Sixty-Five Days of
- 4 Taxable Year.—
- 5 "(1) GENERAL RULE.—If within the first 65
- 6 days of any taxable year of an estate or a trust, an
- 7 amount is properly paid or credited, such amount
- 8 shall be considered paid or credited on the last day
- 9 of the preceding taxable year.
- 10 "(2) LIMITATION.—Paragraph (1) shall apply
- 11 with respect to any taxable year of an estate or a
- trust only if the executor of such estate or the fidu-
- ciary of such trust (as the case may be) elects, in
- such manner and at such time as the Secretary pre-
- scribes by regulations, to have paragraph (1) apply
- for such taxable year.
- 17 "(c) Separate Shares Treated as Separate Es-
- 18 TATES OR TRUSTS.—For the sole purpose of determining
- 19 the amount of distributable net income in the application
- 20 of sections 146 and 147, in the case of a single trust hav-
- 21 ing more than one beneficiary, substantially separate and
- 22 independent shares of different beneficiaries in the trust
- 23 shall be treated as separate trusts. Rules similar to the
- 24 rules of the preceding provisions of this subsection shall
- 25 apply to treat substantially separate and independent

- 1 shares of different beneficiaries in an estate having more
- 2 than 1 beneficiary as separate estates. The existence of
- 3 such substantially separate and independent shares and
- 4 the manner of treatment as separate trusts or estates, in-
- 5 cluding the application of sections 150 through 152, shall
- 6 be determined in accordance with regulations prescribed
- 7 by the Secretary.

8 "SEC. 149. CHARITABLE REMAINDER TRUSTS.

- 9 "(a) GENERAL RULE.—Notwithstanding any other
- 10 provision of this subchapter, the provisions of this section
- 11 shall, in accordance with regulations prescribed by the
- 12 Secretary, apply in the case of a charitable remainder an-
- 13 nuity trust and a charitable remainder unitrust.
- 14 "(b) Character of Distributions.—Amounts dis-
- 15 tributed by a charitable remainder annuity trust or by a
- 16 charitable remainder unitrust shall be considered as hav-
- 17 ing the following characteristics in the hands of a bene-
- 18 ficiary to whom is paid the annuity described in subsection
- 19 (d)(1)(A) or the payment described in subsection
- 20 (d)(2)(A):
- 21 "(1) First, as amounts of income (other than
- gains, and amounts treated as gains, from the sale
- or other disposition of capital assets) includible in
- 24 gross income to the extent of such income of the

1	trust for the year and such undistributed income of
2	the trust for prior years;
3	"(2) Second, as a capital gain to the extent of
4	the capital gain of the trust for the year and the un-
5	distributed capital gain of the trust for prior years;
6	"(3) Third, as other income to the extent of
7	such income of the trust for the year and such un-
8	distributed income of the trust for prior years; and
9	"(4) Fourth, as a distribution of trust corpus.
10	For purposes of this section, the trust shall determine the
11	amount of its undistributed capital gain on a cumulative
12	net basis.
13	"(c) Exemption From Income Taxes.—A chari-
14	table remainder annuity trust and a charitable remainder
15	unitrust shall, for any taxable year, not be subject to any
16	tax imposed by this chapter. Any such trust shall be liable
17	for tax on its unrelated business taxable income (within
18	the meaning of section 255).
19	"(d) Definitions.—
20	"(1) Charitable remainder annuity
21	TRUST.—For purposes of this section, a charitable
22	remainder annuity trust is a trust—
23	"(A) from which a sum certain (which is
24	not less than 5 percent nor more than 50 per-
25	cent of the initial net fair market value of all

property placed in trust) is to be paid, not less often than annually, to one or more persons (at least one of which is not an organization described in section 101(c) and, in the case of individuals, only to an individual who is living at the time of the creation of the trust) for a term of years (not in excess of 20 years) or for the life or lives of such individual or individuals,

"(B) from which no amount other than the payments described in subparagraph (A) and other than qualified gratuitous transfers described in subparagraph (C) may be paid to or for the use of any person other than an organization described in section 101(c),

"(C) following the termination of the payments described in subparagraph (A), the remainder interest in the trust is to be transferred to, or for the use of, an organization described in section 101(c) or is to be retained by the trust for such a use or, to the extent the remainder interest is in qualified employer securities (as defined in subsection (g)(4)), all or part of such securities are to be transferred to an employee stock ownership plan (as defined in

1	section 4975(e)(7) in a qualified gratuitous
2	transfer (as defined by subsection (g)).
3	"(D) the value (determined under section
4	7520 of such remainder interest is at least 10
5	percent of the initial net fair market value of all
6	property placed in the trust.
7	"(2) Charitable remainder unitrust.—For
8	purposes of this section, a charitable remainder
9	unitrust is a trust—
10	"(A) from which a fixed percentage (which
11	is not less than 5 percent nor more than 50
12	percent) of the net fair market value of its as-
13	sets, valued annually, is to be paid, not less
14	often than annually, to one or more persons (at
15	least one of which is not an organization de-
16	scribed in section 101(c) and, in the case of in-
17	dividuals, only to an individual who is living at
18	the time of the creation of the trust) for a term
19	of years (not in excess of 20 years) or for the
20	life or lives of such individual or individuals,
21	"(B) from which no amount other than the
22	payments described in subparagraph (A) and
23	other than qualified gratuitous transfers de-

scribed in subparagraph (C) may be paid to or

for the use of any person other than an organization described in section 101(c),

"(C) following the termination of the payments described in subparagraph (A), the remainder interest in the trust is to be transferred to, or for the use of, an organization described in section 101(c) or is to be retained by the trust for such a use or, to the extent the remainder interest is in qualified employer securities (as defined in subsection (g)(4)), all or part of such securities are to be transferred to an employee stock ownership plan (as defined in section 4975(e)(7) in a qualified gratuitous transfer (as defined by subsection (g)).

"(D) with respect to each contribution of property to the trust, the value (determined under section 7520 of such remainder interest in such property is at least 10 percent of the net fair market value of such property as of the date such property is contributed to the trust.

"(3) EXCEPTION.—Notwithstanding the provisions of paragraphs (2)(A) and (B), the trust instrument may provide that the trustee shall pay the income beneficiary for any year—

1	"(A) the amount of the trust income, if
2	such amount is less than the amount required
3	to be distributed under paragraph (2)(A), and
4	"(B) any amount of the trust income
5	which is in excess of the amount required to be
6	distributed under paragraph (2)(A), to the ex-
7	tent that (by reason of subparagraph (A)) the
8	aggregate of the amounts paid in prior years
9	was less than the aggregate of such required
10	amounts.
11	"(4) SEVERANCE OF CERTAIN ADDITIONAL
12	CONTRIBUTIONS.—If—
13	"(A) any contribution is made to a trust
14	which before the contribution is a charitable re-
15	mainder unitrust, and
16	"(B) such contribution would (but for this
17	paragraph) result in such trust ceasing to be a
18	charitable unitrust by reason of paragraph
19	(2)(D), such contribution shall be treated as a
20	transfer to a separate trust under regulations
21	prescribed by the Secretary.
22	"(e) Valuation for Purposes of Charitable
23	Contribution.—For purposes of determining the
24	amount of any charitable contribution, the remainder in-
25	terest of a charitable remainder annuity trust or charitable

- 1 remainder unitrust shall be computed on the basis that
- 2 an amount equal to 5 percent of the net fair market value
- 3 of its assets (or a greater amount, if required under the
- 4 terms of the trust instrument) is to be distributed each
- 5 year.

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- 6 "(f) CERTAIN CONTINGENCIES PERMITTED.—
- "(1) GENERAL RULE.—If a trust would, but for a qualified contingency, meet the requirements of paragraph (1)(A) or (2)(A) of subsection (d), such trust shall be treated as meeting such requirements.
 - "(2) Value determined without regard to qualified contingency.—For purposes of determining the amount of any charitable contribution (or the actuarial value of any interest), a qualified contingency shall not be taken into account.
 - "(3) QUALIFIED CONTINGENCY.—For purposes of this subsection, the term 'qualified contingency' means any provision of a trust which provides that, upon the happening of a contingency, the payments described in paragraph (1)(A) or (2)(A) of subsection (d) (as the case may be) will terminate not later than such payments would otherwise terminate under the trust.
- 24 "(g) Qualified Gratuitous Transfer of Quali-
- 25 FIED EMPLOYER SECURITIES.—

1	"(1) In general.—For purposes of this sec-
2	tion, the term 'qualified gratuitous transfer' means
3	a transfer of qualified employer securities to an em-
4	ployee stock ownership plan (as defined in section
5	4975(e)(7) but only to the extent that—
6	"(A) the securities transferred previously
7	passed from a decedent dying before January 1,
8	1999, to a trust described in paragraph (1) or
9	(2) of subsection (d),
10	"(B) no deduction under section 404 is al-
11	lowable with respect to such transfer,
12	"(C) such plan contains the provisions re-
13	quired by paragraph (3),
14	"(D) such plan treats such securities as
15	being attributable to employer contributions but
16	without regard to the limitations otherwise ap-
17	plicable to such contributions under section
18	404, and
19	"(E) the employer whose employees are
20	covered by the plan described in this paragraph
21	files with the Secretary a verified written state-
22	ment consenting to the application of sections
23	4978 and 4979A with respect to such employer.
24	"(2) Exception.—The term 'qualified gratu-
25	itous transfer' shall not include a transfer of quali-

1	fied employer securities to an employee stock owner-
2	ship plan unless—
3	"(A) such plan was in existence on August
4	1, 1996,
5	"(B) at the time of the transfer, the dece-
6	dent and members of the decedent's family
7	(within the meaning of section 171(a)(6)(D))
8	own (directly or through constructive ownership
9	rules) no more than 10 percent of the value of
10	the stock of the corporation referred to in para-
11	graph (4), and
12	"(C) immediately after the transfer, such
13	plan owns (after the application of section
14	318(a)(4) at least 60 percent of the value of the
15	outstanding stock of the corporation.
16	"(3) Plan requirements.—A plan contains
17	the provisions required by this paragraph if such
18	plan provides that—
19	"(A) the qualified employer securities so
20	transferred are allocated to plan participants in
21	a manner consistent with section 401(a)(4),
22	"(B) plan participants are entitled to di-
23	rect the plan as to the manner in which such
24	securities which are entitled to vote and are al-

1	located to the account of such participant are to
2	be voted,
3	"(C) an independent trustee votes the se-
4	curities so transferred which are not allocated
5	to plan participants,
6	"(D) each participant who is entitled to a
7	distribution from the plan has the rights de-
8	scribed in subparagraphs (A) and (B) of section
9	409(h)(1),
10	"(E) such securities are held in a suspense
11	account under the plan to be allocated each
12	year, up to the limitations under section 415(c),
13	after first allocating all other annual additions
14	for the limitation year, up to the limitations
15	under sections 415 (c) and (e), and
16	"(F) on termination of the plan, all securi-
17	ties so transferred which are not allocated to
18	plan participants as of such termination are to
19	be transferred to, or for the use of, an organi-
20	zation described in section 101(c). For purposes
21	of the preceding sentence, the term 'independ-
22	ent trustee' means any trustee who is not a
23	member of the family (within the meaning of
24	section $171(a)(6)(D)$) of the decedent or a 5-
25	percent shareholder. A plan shall not fail to be

1	treated as meeting the requirements of section
2	401(a) by reason of meeting the requirements
3	of this subsection.
4	"(4) Qualified employer securities.—For
5	purposes of this section, the term 'qualified employer
6	securities' means employer securities (as defined in
7	section 409(l)) which are issued by a domestic
8	corporation—
9	"(A) which has no outstanding stock which
10	is readily tradable on an established securities
11	market, and
12	"(B) which has only 1 class of stock.
13	"(5) Treatment of securities allocated
14	BY EMPLOYEE STOCK OWNERSHIP PLAN TO PER-
15	SONS RELATED TO DECEDENT OR 5-PERCENT
16	SHAREHOLDERS.—
17	"(A) IN GENERAL.—If any portion of the
18	assets of the plan attributable to securities ac-
19	quired by the plan in a qualified gratuitous
20	transfer are allocated to the account of—
21	"(i) any person who is related to the
22	decedent (within the meaning of section
23	171(a)(5) or a member of the decedent's
24	family (within the meaning of section
25	171(a)(6)(D), or

1	"(ii) any person who, at the time of
2	such allocation or at any time during the
3	1-year period ending on the date of the ac-
4	quisition of qualified employer securities by
5	the plan, is a 5-percent shareholder of the
6	employer maintaining the plan, the plan
7	shall be treated as having distributed (at
8	the time of such allocation) to such person
9	or shareholder the amount so allocated.
10	"(B) 5-PERCENT SHAREHOLDER.—For
11	purposes of subparagraph (A), the term '5-per-
12	cent shareholder' means any person who owns
13	(directly or through the application of construc-
14	tive ownership rules) more than 5 percent of
15	the outstanding stock of the corporation which
16	issued such qualified employer securities or of
17	any corporation which is a member of the same
18	controlled group of corporations (within the
19	meaning of section 409(l)(4)) as such corpora-
20	tion.
21	"(C) Cross reference.—For excise tax
22	on allocations described in subparagraph (A)
23	see section 4979A.

"(6) Tax on failure to transfer

UNALLOCATED SECURITIES TO CHARITY ON TERMI-

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1	NATION OF PLAN.—If the requirements of paragraph
2	(3)(F) are not met with respect to any securities,
3	there is hereby imposed a tax on the employer main-
4	taining the plan in an amount equal to the sum of—
5	"(A) the amount of the increase in the tax
6	which would be imposed by chapter 11 if such
7	securities were not transferred as described in
8	paragraph (1), and
9	"(B) interest on such amount at the un-
10	derpayment rate under section 6621 (and com-
11	pounded daily) from the due date for filing the
12	return of the tax imposed by chapter 11.
13	"SEC. 150. DEFINITIONS APPLICABLE TO EXCESS DISTRIBU-
13 14	"SEC. 150. DEFINITIONS APPLICABLE TO EXCESS DISTRIBU- TION RULES.
14	TION RULES.
141516	TION RULES. "(a) Undistributed Net Income.—For purposes
14 15 16 17	TION RULES. "(a) Undistributed Net Income.—For purposes of sections 150 through 152, the term 'undistributed net
14 15 16 17 18	"(a) Undistributed Net Income.—For purposes of sections 150 through 152, the term 'undistributed net income' for any taxable year means the amount by which
14 15 16 17 18	"(a) Undistributed Net Income.—For purposes of sections 150 through 152, the term 'undistributed net income' for any taxable year means the amount by which the distributable net income of the trust for such taxable
14 15 16 17 18	"(a) Undistributed Net Income.—For purposes of sections 150 through 152, the term 'undistributed net income' for any taxable year means the amount by which the distributable net income of the trust for such taxable year exceeds the sum of—
14 15 16 17 18 19 20	"(a) Undistributed Net Income.—For purposes of sections 150 through 152, the term 'undistributed net income' for any taxable year means the amount by which the distributable net income of the trust for such taxable year exceeds the sum of— "(1) the amounts for such taxable year speci-
14 15 16 17 18 19 20 21	"(a) Undistributed Net Income.—For purposes of sections 150 through 152, the term 'undistributed net income' for any taxable year means the amount by which the distributable net income of the trust for such taxable year exceeds the sum of— "(1) the amounts for such taxable year specified in paragraphs (1) and (2) of section 146(a),

- 1 "(b) ACCUMULATION DISTRIBUTION.—For purposes
- 2 of sections 150 through 152, except as provided in sub-
- 3 section (c), the term 'accumulation distribution' means,
- 4 for any taxable year of the trust, the amount by which—
- 5 "(1) the amounts specified in paragraph (2) of
- 6 section 146(a) for such taxable year, exceed
- 7 "(2) distributable net income for such year re-
- 8 duced (but not below zero) by the amounts specified
- 9 in paragraph (1) of section 146(a).
- 10 For purposes of section 152 (other than subsection (c)
- 11 thereof, relating to multiple trusts), the amounts specified
- 12 in paragraph (2) of section 146(a) shall not include
- 13 amounts properly paid, credited, or required to be distrib-
- 14 uted to a beneficiary from a trust (other than a foreign
- 15 trust) as income accumulated before the birth of such ben-
- 16 eficiary or before such beneficiary attains the age of 21.
- 17 If the amounts properly paid, credited, or required to be
- 18 distributed by the trust for the taxable year do not exceed
- 19 the income of the trust for such year, there shall be no
- 20 accumulation distribution for such year.
- 21 "(c) Exception for Accumulation Distribu-
- 22 TIONS FROM CERTAIN DOMESTIC TRUSTS.—For purposes
- 23 of sections 150 through 152—
- 24 "(1) IN GENERAL.—In the case of a qualified
- 25 trust, any distribution in any taxable year beginning

1	after the date of the enactment of this subsection
2	shall be computed without regard to any undistrib-
3	uted net income.
4	"(2) Qualified trust.—For purposes of this
5	subsection, the term 'qualified trust' means any
6	trust other than—
7	"(A) a foreign trust (or, except as provided
8	in regulations, a domestic trust which at any
9	time was a foreign trust), or
10	"(B) a trust created before March 1, 1984,
11	unless it is established that the trust would not
12	be aggregated with other trusts under section
13	143(f) if such section applied to such trust.
14	"(d) Taxes Imposed on the Trust.—For purposes
15	of sections 150 through 152—
16	"(1) In general.—The term 'taxes imposed
17	on the trust' means the amount of the taxes which
18	are imposed for any taxable year of the trust under
19	this chapter (without regard to sections 150 through
20	152) and which, under regulations prescribed by the
21	Secretary, are properly allocable to the undistributed
22	portions of distributable net income and gains in ex-
23	cess of losses from sales or exchanges of capital as-
24	sets. The amount determined in the preceding sen-
25	tence shall be reduced by any amount of such taxes

deemed distributed under section 151(b) and (c) to any beneficiary.

"(2) Foreign trusts.—In the case of any foreign trust, the term 'taxes imposed on the trust' includes the amount, reduced as provided in the last sentence of paragraph (1), of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on such foreign trust which, as determined under paragraph (1), are so properly allocable. Under rules or regulations prescribed by the Secretary, in the case of any foreign trust of which the settlor or another person would be treated as owner of any portion of the trust but for section 154(f), the term 'taxes imposed on the trust' includes the allocable amount of any income, war profits, and excess profits taxes imposed by any foreign country or possession of the United States on the settlor or such other person in respect of trust income.

20 "SEC. 151. ACCUMULATION DISTRIBUTION ALLOCATED TO

21 PRECEDING YEARS.

"(a) Amount Allocated.—In the case of a trust which is subject to sections 146 through 149, the amount of the accumulation distribution of such trust for a taxable year shall be deemed to be an amount within the meaning

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- 1 of paragraph (2) of section 146(a) distributed on the last
- 2 day of each of the preceding taxable years, commencing
- 3 with the earliest of such years, to the extent that such
- 4 amount exceeds the total of any undistributed net income
- 5 for all earlier preceding taxable years. The amount deemed
- 6 to be distributed in any such preceding taxable year under
- 7 the preceding sentence shall not exceed the undistributed
- 8 net income for such preceding taxable year. For purposes
- 9 of this subsection, undistributed net income for each of
- 10 such preceding taxable years shall be computed without
- 11 regard to such accumulation distribution and without re-
- 12 gard to any accumulation distribution determined for any
- 13 succeeding taxable year.
- 14 "(b) Total Taxes Deemed Distributed.—If any
- 15 portion of an accumulation distribution for any taxable
- 16 year is deemed under subsection (a) to be an amount with-
- 17 in the meaning of paragraph (2) of section 146(a) distrib-
- 18 uted on the last day of any preceding taxable year, and
- 19 such portion of such distribution is not less than the un-
- 20 distributed net income for such preceding taxable year, the
- 21 trust shall be deemed to have distributed on the last day
- 22 of such preceding taxable year an additional amount with-
- 23 in the meaning of paragraph (2) of section 146(a). Such
- 24 additional amount shall be equal to the taxes imposed on
- 25 the trust for such preceding taxable year attributable to

- 1 the undistributed net income. For purposes of this sub-
- 2 section, the undistributed net income and the taxes im-
- 3 posed on the trust for such preceding taxable year attrib-
- 4 utable to such undistributed net income shall be computed
- 5 without regard to such accumulation distribution and
- 6 without regard to any accumulation distribution deter-
- 7 mined for any succeeding taxable year.
- 8 "(c) Pro Rata Portion of Taxes Deemed Dis-
- 9 TRIBUTED.—If any portion of an accumulation distribu-
- 10 tion for any taxable year is deemed under subsection (a)
- 11 to be an amount within the meaning of paragraph (2) of
- 12 section 146(a) distributed on the last day of any preceding
- 13 taxable year and such portion of the accumulation dis-
- 14 tribution is less than the undistributed net income for such
- 15 preceding taxable year, the trust shall be deemed to have
- 16 distributed on the last day of such preceding taxable year
- 17 an additional amount within the meaning of paragraph (2)
- 18 of section 146(a). Such additional amount shall be equal
- 19 to the taxes imposed on the trust for such taxable year
- 20 attributable to the undistributed net income multiplied by
- 21 the ratio of the portion of the accumulation distribution
- 22 to the undistributed net income of the trust for such year.
- 23 For purposes of this subsection, the undistributed net in-
- 24 come and the taxes imposed on the trust for such preced-
- 25 ing taxable year attributable to such undistributed net in-

- 1 come shall be computed without regard to the accumula-
- 2 tion distribution and without regard to any accumulation
- 3 distribution determined for any succeeding taxable year.
- 4 "(d) Rule When Information Is Not Avail-
- 5 ABLE.—If adequate records are not available to determine
- 6 the proper application of this subchapter to an amount
- 7 distributed by a trust, such amount shall be deemed to
- 8 be an accumulation distribution consisting of undistrib-
- 9 uted net income earned during the earliest preceding tax-
- 10 able year of the trust in which it can be established that
- 11 the trust was in existence.
- 12 "(e) Denial of Refund to Trusts and Bene-
- 13 FICIARIES.—No refund or credit shall be allowed to a trust
- 14 or a beneficiary of such trust for any preceding taxable
- 15 year by reason of a distribution deemed to have been made
- 16 by such trust in such year under this section.
- 17 "SEC. 152. TREATMENT OF AMOUNTS DEEMED DISTRIB-
- 18 UTED BY TRUST IN PRECEDING YEARS.
- 19 "(a) General Rule.—The total of the amounts
- 20 which are treated under section 151 as having been dis-
- 21 tributed by a trust in a preceding taxable year shall be
- 22 included in the income of a beneficiary of the trust when
- 23 paid, credited, or required to be distributed to the extent
- 24 that such total would have been included in the income
- 25 of such beneficiary under section 147(a)(2) (and, with re-

1	spect to any tax-exempt interest to which section 103 ap-
2	plies, under section 147(b)) if such total had been paid
3	to such beneficiary on the last day of such preceding tax-
4	able year. The tax imposed by this subtitle on a beneficiary
5	for a taxable year in which any such amount is included
6	in his income shall be determined only as provided in this
7	section and shall consist of the sum of—
8	"(1) a partial tax computed on the taxable in-
9	come reduced by an amount equal to the total of
10	such amounts, at the rate and in the manner as if
11	this section had not been enacted,
12	"(2) a partial tax determined as provided in
13	subsection (b) of this section, and
14	"(3) in the case of a foreign trust, the interest
15	charge determined as provided in section 152.
16	"(b) Tax on Distribution.—
17	"(1) In general.—The partial tax imposed by
18	subsection (a)(2) shall be determined.
19	"(A) by determining the number of preced-
20	ing taxable years of the trust on the last day
21	of which an amount is deemed under section
22	151(a) to have been distributed,
23	"(B) by taking from the 5 taxable years
24	immediately preceding the year of the accumu-
25	lation distribution the 1 tayable year for which

1	the beneficiary's taxable income was the highest
2	and the 1 taxable year for which his taxable in-
3	come was the lowest,
4	"(C) by adding to the beneficiary's taxable
5	income for each of the 3 taxable years remain-
6	ing after the application of subparagraph (B)
7	an amount determined by dividing the amount
8	deemed distributed under section 151 and re-
9	quired to be included in income under sub-
10	section (a) by the number of preceding taxable
11	years determined under subparagraph (A), and
12	"(D) by determining the average increase
13	in tax for the 3 taxable years referred to in sub-
14	paragraph (C) resulting from the application of
15	such subparagraph.
16	The partial tax imposed by subsection (a)(2) shall be
17	the excess (if any) of the average increase in tax de-
18	termined under subparagraph (D), multiplied by the
19	number of preceding taxable years determined under
20	subparagraph (A), over the amount of taxes (other
21	than the amount of taxes described in section
22	150(d)(2)) deemed distributed to the beneficiary
23	under sections 151 (b) and (c).
24	"(2) Treatment of loss years.—For pur-
25	poses of paragraph (1), the taxable income of the

- beneficiary for any taxable year shall be deemed to
 be not less than zero.
- "(3) CERTAIN PRECEDING TAXABLE YEARS NOT 3 TAKEN INTO ACCOUNT.—For purposes of paragraph 5 (1), if the amount of the undistributed net income deemed distributed in any preceding taxable year of 6 7 the trust is less than 25 percent of the amount of 8 the accumulation distribution divided by the number 9 of preceding taxable years to which the accumulation 10 distribution is allocated under section 151(a), the 11 number of preceding taxable years of the trust with 12 respect to which an amount is deemed distributed to 13 a beneficiary under section 151(a) shall be deter-14 mined without regard to such year.
 - "(4) EFFECT OF OTHER ACCUMULATION DISTRIBUTIONS.—In computing the partial tax under paragraph (1) for any beneficiary, the income of such beneficiary for each of his prior taxable years shall include amounts previously deemed distributed to such beneficiary in such year under section 151 as a result of prior accumulation distributions (whether from the same or another trust).
 - "(5) MULTIPLE DISTRIBUTIONS IN THE SAME TAXABLE YEAR.—In the case of accumulation distributions made from more than one trust which are

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includible in the income of a beneficiary in the same taxable year, the distributions shall be deemed to have been made consecutively in whichever order the beneficiary shall determine. Generation-skipping transfer bears to the total accumulation distribution.

"(c) Special Rule for Multiple Trusts.—

"(1) In General.—If, in the same prior taxable year of the beneficiary in which any part of the accumulation distribution from a trust (hereinafter in this paragraph referred to as "third trust") is deemed under section 151(a) to have been distributed to such beneficiary, some part of prior distributions by each of 2 or more other trusts is deemed under section 151(a) to have been distributed to such beneficiary, then subsections (b) and (c) of section 151 shall not apply with respect to such part of the accumulation distribution from such third trust.

"(2) Accumulation distributions from trust not taken into account unless they equal or exceed \$1,000.—For purposes of paragraph (1), an accumulation distribution from a trust to a beneficiary shall be taken into account only if such distribution, when added to any prior accumulation distributions from such trust which are

1	deemed	under	section	151(a)	to	have	been	distrib-
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- 2 uted to such beneficiary for the same prior taxable
- 3 year of the beneficiary, equals or exceeds \$1,000.
- 4 "SEC. 153. TRUST INCOME, DEDUCTIONS, AND CREDITS AT-
- 5 TRIBUTABLE TO GRANTORS AND OTHERS AS
- 6 SUBSTANTIAL OWNERS.
- 7 "Where it is specified in sections 153 through 161
- 8 that the grantor or another person shall be treated as the
- 9 owner of any portion of a trust, there shall then be in-
- 10 cluded in computing the taxable income and credits of the
- 11 grantor or the other person those items of income, deduc-
- 12 tions, and credits against tax of the trust which are attrib-
- 13 utable to that portion of the trust to the extent that such
- 14 items would be taken into account under this chapter in
- 15 computing taxable income or credits against the tax of an
- 16 individual. Any remaining portion of the trust shall be
- 17 subject to sections 140 through 152. No items of a trust
- 18 shall be included in computing the taxable income and
- 19 credits of the grantor or of any other person solely on the
- 20 grounds of his dominion and control over the trust under
- 21 section 61 (relating to definition of gross income) or any
- 22 other provision of this title, except as specified in this sub-
- 23 part.

1 "SEC. 154. DEFINITIONS AND RULES.

2 "(a) Adverse	Party.—I	For purposes	of	sections	15	58	3
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- 3 through 160, 'adverse party' means any person having a
- 4 substantial beneficial interest in the trust which would be
- 5 adversely affected by the exercise or nonexercise of the
- 6 power which he possesses respecting the trust. A person
- 7 having a general power of appointment over the trust
- 8 property shall be deemed to have a beneficial interest in
- 9 the trust.
- 10 "(b) Nonadverse Party.—For purposes of sections
- 11 153 through 160, 'nonadverse party' means any person
- 12 who is not an adverse party.
- 13 "(c) Related or Subordinate Party.—For pur-
- 14 poses of sections 153 through 161, 'related or subordinate
- 15 party' means any nonadverse party who is—
- 16 "(1) the grantor's spouse if living with the
- 17 grantor;
- 18 "(2) any one of the following: The grantor's fa-
- ther, mother, issue, brother or sister; an employee of
- the grantor; a corporation or any employee of a cor-
- 21 poration in which the stock holdings of the grantor
- and the trust are significant from the viewpoint of
- voting control; a subordinate employee of a corpora-
- tion in which the grantor is an executive.
- 25 For purposes of subsection (f) and sections 156 and 157,
- 26 a related or subordinate party shall be presumed to be

1	subservient to the grantor in respect of the exercise or
2	nonexercise of the powers conferred on him unless such
3	party is shown not to be subservient by a preponderance
4	of the evidence.
5	"(d) Rule Where Power Is Subject to Condi-
6	TION PRECEDENT.—A person shall be considered to have
7	a power described in sections 153 through 161 even
8	though the exercise of the power is subject to a precedent
9	giving of notice or takes effect only on the expiration of
10	a certain period after the exercise of the power.
11	"(e) Grantor Treated as Holding Any Power
12	OR INTEREST OF GRANTOR'S SPOUSE.—
13	"(1) In general.—For purposes of sections
14	153 through 160, a grantor shall be treated as hold-
15	ing any power or interest held by—
16	"(A) any individual who was the spouse of
17	the grantor at the time of the creation of such
18	power or interest, or
19	"(B) any individual who became the spouse
20	of the grantor after the creation of such power
21	or interest, but only with respect to periods
22	after such individual became the spouse of the
23	grantor.
24	"(2) Marital Status.—For purposes of para-
25	graph (1)(A), an individual legally separated from

1	his spouse under a decree of divorce or of separate
2	maintenance shall not be considered as married.
3	"(f) Rules Not To Result in Foreign Owner-
4	SHIP.—
5	"(1) In general.—Notwithstanding any other
6	provision in sections 153 through 160, sections 153
7	through 160 shall apply only to the extent such ap-
8	plication results in an amount (if any) being cur-
9	rently taken into account (directly or through 1 or
10	more entities) under this chapter in computing the
11	income of a citizen or resident of the United States
12	or a domestic corporation.
13	"(2) Exceptions.—
14	"(A) CERTAIN REVOCABLE AND IRREV-
15	OCABLE TRUSTS.—Paragraph (1) shall not
16	apply to any portion of a trust if—
17	"(i) the power to revest absolutely in
18	the grantor title to the trust property to
19	which such portion is attributable is exer-
20	cisable solely by the grantor without the
21	approval or consent of any other person or
22	with the consent of a related or subordi-
23	nate party who is subservient to the grant-
24	or, or

1	"(ii) the only amounts distributable
2	from such portion (whether income or cor-
3	pus) during the lifetime of the grantor are
4	amounts distributable to the grantor or the
5	spouse of the grantor.
6	"(B) Compensatory trusts.—Except as
7	provided in regulations, paragraph (1) shall not
8	apply to any portion of a trust distributions
9	from which are taxable as compensation for
10	services rendered.
11	"(3) Special rules.—Except as otherwise
12	provided in regulations prescribed by the Secretary,
13	a controlled foreign corporation shall be treated as
14	a domestic corporation for purposes of paragraph
15	(1).
16	"(4) Recharacterization of purported
17	GIFTS.—In the case of any transfer directly or indi-
18	rectly from a partnership or foreign corporation
19	which the transferee treats as a gift or bequest, the
20	Secretary may recharacterize such transfer in such
21	circumstances as the Secretary determines to be ap-
22	propriate to prevent the avoidance of the purposes of
23	this subsection.
24	"(5) Special rule where grantor is for-
25	EIGN PERSON.—If—

1	"(A) but for this subsection, a foreign per-
2	son would be treated as the owner of any por-
3	tion of a trust, and
4	"(B) such trust has a beneficiary who is a
5	United States person,
6	such beneficiary shall be treated as the grantor of
7	such portion to the extent such beneficiary has made
8	(directly or indirectly) transfers of property (other
9	than in a sale for full and adequate consideration)
10	to such foreign person.
11	"(6) Regulations.—The Secretary shall pre-
12	scribe such regulations as may be necessary or ap-
13	propriate to carry out the purposes of this sub-
14	section, including regulations providing that para-
15	graph (1) shall not apply in appropriate cases.
16	"SEC. 155. REVERSIONARY INTERESTS.
17	"(a) General Rule.—The grantor shall be treated
18	as the owner of any portion of a trust in which he has
19	a reversionary interest in either the corpus or the income
20	therefrom, if, as of the inception of that portion of the
21	trust, the value of such interest exceeds 5 percent of the
22	value of such portion.
23	"(b) Reversionary Interest Taking Effect at
24	DEATH OF MINOR LINEAL DESCENDANT BENE-
25	FICIARY.—In the case of any beneficiary who—

- 1 "(1) is a lineal descendant of the grantor, and
- 2 "(2) holds all of the present interests in any
- 3 portion of a trust,
- 4 the grantor shall not be treated under subsection (a) as
- 5 the owner of such portion solely by reason of a reversion-
- 6 ary interest in such portion which takes effect upon the
- 7 death of such beneficiary before such beneficiary attains
- 8 age 21.
- 9 "(c) Special Rule for Determining Value of
- 10 REVERSIONARY INTEREST.—For purposes of subsection
- 11 (a), the value of the grantor's reversionary interest shall
- 12 be determined by assuming the maximum exercise of dis-
- 13 cretion in favor of the grantor.
- 14 "(d) Postponement of Date Specified for Re-
- 15 ACQUISITION.—Any postponement of the date specified for
- 16 the reacquisition of possession or enjoyment of the rever-
- 17 sionary interest shall be treated as a new transfer in trust
- 18 commencing with the date on which the postponement is
- 19 effective and terminating with the date prescribed by the
- 20 postponement. However, income for any period shall not
- 21 be included in the income of the grantor by reason of the
- 22 preceding sentence if such income would not be so includ-
- 23 ible in the absence of such postponement.

1 "SEC. 156. POWER TO CONTROL BENEFICIAL ENJOYMENT.

- 2 "(a) GENERAL RULE.—The grantor shall be treated
- 3 as the owner of any portion of a trust in respect of which
- 4 the beneficial enjoyment of the corpus or the income there-
- 5 from is subject to a power of disposition, exercisable by
- 6 the grantor or a nonadverse party, or both, without the
- 7 approval or consent of any adverse party.
- 8 "(b) Exceptions for Certain Powers.—Sub-
- 9 section (a) shall not apply to the following powers regard-
- 10 less of by whom held:
- 11 "(1) Power to apply income to support of
- 12 A DEPENDENT.—A power described in section
- 13 159(b) to the extent that the grantor would not be
- subject to tax under that section.
- 15 "(2) Power affecting beneficial enjoy-
- MENT ONLY AFTER OCCURRENCE OF EVENT.—A
- power, the exercise of which can only affect the ben-
- eficial enjoyment of the income for a period com-
- mencing after the occurrence of an event such that
- a grantor would not be treated as the owner under
- section 155 if the power were a reversionary inter-
- est; but the grantor may be treated as the owner
- after the occurrence of the event unless the power is
- relinquished.
- 25 "(3) Power exercisable only by will.—A
- power exercisable only by will, other than a power in

the grantor to appoint by will the income of the trust where the income is accumulated for such disposition by the grantor or may be so accumulated in the discretion of the grantor or a nonadverse party, or both, without the approval or consent of any adverse party.

- "(4) Power to allocate among charitable Beneficial enjoyment of the corpus or the income thereficial enjoyment of the corpus or the income therefrom if the corpus or income is irrevocably payable for a purpose specified in section 101(c) (relating to definition of charitable contributions) or to an employee stock ownership plan (as defined in section 4975(e)(7)) in a qualified gratuitous transfer (as defined in section 149(g)(1)).
- "(5) Power to distribute corpus either—
 - "(A) to or for a beneficiary or beneficiaries or to or for a class of beneficiaries (whether or not income beneficiaries) provided that the power is limited by a reasonably definite standard which is set forth in the trust instrument; or
- 24 "(B) to or for any current income bene-25 ficiary, provided that the distribution of corpus

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1 must be chargeable against the proportionate 2 share of corpus held in trust for the payment 3 of income to the beneficiary as if the corpus 4 constituted a separate trust.

> A power does not fall within the powers described in this paragraph if any person has a power to add to the beneficiary or beneficiaries or to a class of beneficiaries designated to receive the income or corpus, except where such action is to provide for after-born or after-adopted children.

> "(6) Power to withhold income tempo-Rarily.—A power to distribute or apply income to or for any current income beneficiary or to accumulate the income for him, provided that any accumulated income must ultimately be payable—

"(A) to the beneficiary from whom distribution or application is withheld, to his estate, or to his appointees (or persons named as alternate takers in default of appointment) provided that such beneficiary possesses a power of appointment which does not exclude from the class of possible appointees any person other than the beneficiary, his estate, his creditors, or the creditors of his estate, or

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1 "(B) on termination of the trust, or in con2 junction with a distribution of corpus which is
3 augmented by such accumulated income, to the
4 current income beneficiaries in shares which
5 have been irrevocably specified in the trust in6 strument.

Accumulated income shall be considered so payable although it is provided that if any beneficiary does not survive a date of distribution which could reasonably have been expected to occur within the beneficiary's lifetime, the share of the deceased beneficiary is to be paid to his appointees or to one or more designated alternate takers (other than the grantor or the grantor's estate) whose shares have been irrevocably specified. A power does not fall within the powers described in this paragraph if any person has a power to add to the beneficiary or beneficiaries or to a class of beneficiaries designated to receive the income or corpus except where such action is to provide for after-born or after-adopted children.

"(7) Power to withhold income during disability of a beneficiary.—A power exercisable only during—

1	"(A) the existence of a legal disability of
2	any current income beneficiary, or
3	"(B) the period during which any income
4	beneficiary shall be under the age of 21 years,
5	to distribute or apply income to or for such bene-
6	ficiary or to accumulate and add the income to cor-
7	pus. A power does not fall within the powers de-
8	scribed in this paragraph if any person has a power
9	to add to the beneficiary or beneficiaries or to a
10	class of beneficiaries designated to receive the in-
11	come or corpus, except where such action is to pro-
12	vide for after-born or after-adopted children.
13	"(8) Power to allocate between corpus
14	AND INCOME.—A power to allocate receipts and dis-
15	bursements as between corpus and income, even
16	though expressed in broad language.
17	"(c) Exception for Certain Powers of Inde-
18	PENDENT TRUSTEES.—Subsection (a) shall not apply to
19	a power solely exercisable (without the approval or consent
20	of any other person) by a trustee or trustees, none of
21	whom is the grantor, and no more than half of whom are
22	related or subordinate parties who are subservient to the
23	wishes of the grantor—

- 1 "(1) to distribute, apportion, or accumulate in-2 come to or for a beneficiary or beneficiaries, or to, 3 for, or within a class of beneficiaries; or
- 4 "(2) to pay out corpus to or for a beneficiary 5 or beneficiaries or to or for a class of beneficiaries 6 (whether or not income beneficiaries).
- 7 A power does not fall within the powers described in this
- 8 subsection if any person has a power to add to the bene-
- 9 ficiary or beneficiaries or to a class of beneficiaries des-
- 10 ignated to receive the income or corpus, except where such
- 11 action is to provide for after-born or after-adopted chil-
- 12 dren. For periods during which an individual is the spouse
- 13 of the grantor (within the meaning of section 154(e)(2)),
- 14 any reference in this subsection to the grantor shall be
- 15 treated as including a reference to such individual.
- 16 "(d) Power To Allocate Income if Limited by
- 17 A STANDARD.—Subsection (a) shall not apply to a power
- 18 solely exercisable (without the approval or consent of any
- 19 other person) by a trustee or trustees, none of whom is
- 20 the grantor or spouse living with the grantor, to distribute,
- 21 apportion, or accumulate income to or for a beneficiary
- 22 or beneficiaries, or to, for, or within a class of bene-
- 23 ficiaries, whether or not the conditions of paragraph (6)
- 24 or (7) of subsection (b) are satisfied, if such power is lim-
- 25 ited by a reasonably definite external standard which is

- 1 set forth in the trust instrument. A power does not fall
- 2 within the powers described in this subsection if any per-
- 3 son has a power to add to the beneficiary or beneficiaries
- 4 or to a class of beneficiaries designated to receive the in-
- 5 come or corpus except where such action is to provide for
- 6 after-born or after-adopted children.

7 "SEC. 157. ADMINISTRATIVE POWERS.

- 8 "The grantor shall be treated as the owner of any
- 9 portion of a trust in respect of which—
- 10 "(1) Power to deal for less than ade-
- 11 QUATE AND FULL CONSIDERATION.—A power exer-
- cisable by the grantor or a nonadverse party, or
- both, without the approval or consent of any adverse
- party enables the grantor or any person to purchase,
- exchange, or otherwise deal with or dispose of the
- 16 corpus or the income therefrom for less than an ade-
- 17 quate consideration in money or money's worth.
- 18 "(2) Power to Borrow without adequate
- 19 INTEREST OR SECURITY.—A power exercisable by
- 20 the grantor or a nonadverse party, or both, enables
- 21 the grantor to borrow the corpus or income, directly
- or indirectly, without adequate interest or without
- adequate security except where a trustee (other than
- the grantor) is authorized under a general lending

power to make loans to any person without regard
 to interest or security.

"(3) Borrowing of the trust funds.—The grantor has directly or indirectly borrowed the corpus or income and has not completely repaid the loan, including any interest, before the beginning of the taxable year. The preceding sentence shall not apply to a loan which provides for adequate interest and adequate security, if such loan is made by a trustee other than the grantor and other than a related or subordinate trustee subservient to the grantor. For periods during which an individual is the spouse of the grantor (within the meaning of section 154(e)(2)), any reference in this paragraph to the grantor shall be treated as including a reference to such individual.

"(4) GENERAL POWERS OF ADMINISTRATION.—
A power of administration is exercisable in a nonfiduciary capacity by any person without the approval or consent of any person in a fiduciary capacity. For purposes of this paragraph, the term 'power
of administration' means any one or more of the following powers: (A) a power to vote or direct the voting of stock or other securities of a corporation in
which the holdings of the grantor and the trust are

- 1 significant from the viewpoint of voting control; (B) a power to control the investment of the trust funds 2 3 either by directing investments or reinvestments, or by vetoing proposed investments or reinvestments, to 5 the extent that the trust funds consist of stocks or 6 securities of corporations in which the holdings of 7 the grantor and the trust are significant from the 8 viewpoint of voting control; or (C) a power to reac-9 quire the trust corpus by substituting other property 10 of an equivalent value.
- 11 "SEC. 158. POWER TO REVOKE.
- 12 "(a) General Rule.—The grantor shall be treated
- 13 as the owner of any portion of a trust, whether or not
- 14 he is treated as such owner under any other provision of
- 15 this part, where at any time the power to revest in the
- 16 grantor title to such portion is exercisable by the grantor
- 17 or a non-adverse party, or both.
- 18 "(b) Power Affecting Beneficial Enjoyment
- 19 Only After Occurrence of Event.—Subsection (a)
- 20 shall not apply to a power the exercise of which can only
- 21 affect the beneficial enjoyment of the income for a period
- 22 commencing after the occurrence of an event such that
- 23 a grantor would not be treated as the owner under section
- 24 155 if the power were a reversionary interest. But the

- 1 grantor may be treated as the owner after the occurrence
- 2 of such event unless the power is relinquished.
- 3 "SEC. 159. INCOME FOR BENEFIT OF GRANTOR.
- 4 "(a) General Rule.—The grantor shall be treated
- 5 as the owner of any portion of a trust, whether or not
- 6 he is treated as such owner under section 156, whose in-
- 7 come without the approval or consent of any adverse party
- 8 is, or, in the discretion of the grantor or a nonadverse
- 9 party, or both, may be—
- 10 "(1) distributed to the grantor or the grantor's
- 11 spouse;
- 12 "(2) held or accumulated for future distribution
- to the grantor or the grantor's spouse; or
- "(3) applied to the payment of premiums on
- policies of insurance on the life of the grantor or the
- grantor's spouse (except policies of insurance irrev-
- ocably payable for a purpose specified in section
- 18 101(c) (relating to definition of charitable contribu-
- 19 tions)).
- 20 This subsection shall not apply to a power the exercise
- 21 of which can only affect the beneficial enjoyment of the
- 22 income for a period commencing after the occurrence of
- 23 an event such that the grantor would not be treated as
- 24 the owner under section 153 if the power were a reversion-
- 25 ary interest; but the grantor may be treated as the owner

- 1 after the occurrence of the event unless the power is relin-
- 2 quished.
- 3 "(b) Obligations of Support.—Income of a trust
- 4 shall not be considered taxable to the grantor under sub-
- 5 section (a) or any other provision of this chapter merely
- 6 because such income in the discretion of another person,
- 7 the trustee, or the grantor acting as trustee or co-trustee,
- 8 may be applied or distributed for the support or mainte-
- 9 nance of a beneficiary (other than the grantor's spouse)
- 10 whom the grantor is legally obligated to support or main-
- 11 tain, except to the extent that such income is so applied
- 12 or distributed. In cases where the amounts so applied or
- 13 distributed are paid out of corpus or out of other than
- 14 income for the taxable year, such amounts shall be consid-
- 15 ered to be an amount paid or credited within the meaning
- 16 of paragraph (2) of section 146(a) and shall be taxed to
- 17 the grantor under section 147.
- 18 "SEC. 160. PERSON OTHER THAN GRANTOR TREATED AS
- 19 SUBSTANTIAL OWNER.
- 20 "(a) GENERAL RULE.—A person other than the
- 21 grantor shall be treated as the owner of any portion of
- 22 a trust with respect to which:
- 23 "(1) such person has a power exercisable solely
- by himself to vest the corpus or the income there-
- 25 from in himself, or

- 1 "(2) such person has previously partially re-
- 2 leased or otherwise modified such a power and after
- 3 the release or modification retains such control as
- 4 would, within the principles of sections 153 to 159,
- 5 inclusive, subject a grantor of a trust to treatment
- 6 as the owner thereof.
- 7 "(b) Exception Where Grantor Is Taxable.—
- 8 Subsection (a) shall not apply with respect to a power over
- 9 income, as originally granted or thereafter modified, if the
- 10 grantor of the trust or a transferor (to whom section 161
- 11 applies) is otherwise treated as the owner under sections
- 12 153 through 159 or section 161.
- 13 "(c) Obligations of Support.—Subsection (a)
- 14 shall not apply to a power which enables such person, in
- 15 the capacity of trustee or cotrustee, merely to apply the
- 16 income of the trust to the support or maintenance of a
- 17 person whom the holder of the power is obligated to sup-
- 18 port or maintain except to the extent that such income
- 19 is so applied. In cases where the amounts so applied or
- 20 distributed are paid out of corpus or out of other than
- 21 income of the taxable year, such amounts shall be consid-
- 22 ered to be an amount paid or credited within the meaning
- 23 of paragraph (2) of section 146(a) and shall be taxed to
- 24 the holder of the power under section 147.

1	"(d) Effect of Renunciation or Disclaimer.—
2	Subsection (a) shall not apply with respect to a power
3	which has been renounced or disclaimed within a reason-
4	able time after the holder of the power first became aware
5	of its existence.
6	"SEC. 161. FOREIGN TRUSTS HAVING ONE OR MORE
7	UNITED STATES BENEFICIARIES.
8	"(a) Transferor Treated as Owner.—
9	"(1) In General.—A United States person
10	who directly or indirectly transfers property to a for-
11	eign trust (other than a trust described in section
12	6048(a)(3)(B)(ii)) shall be treated as the owner for
13	his taxable year of the portion of such trust attrib-
14	utable to such property if for such year there is a
15	United States beneficiary of any portion of such
16	trust.
17	"(2) Exceptions.—Paragraph (1) shall not
18	apply—
19	"(A) Transfers by reason of death.—
20	To any transfer by reason of the death of the
21	transferor.
22	"(B) Transfers at fair market
23	VALUE.—To any transfer of property to a trust
24	in exchange for consideration of at least the fair
25	market value of the transferred property. For

1	purposes of the preceding sentence, consider-
2	ation other than cash shall be taken into ac-
3	count at its fair market value.
4	"(3) CERTAIN OBLIGATIONS NOT TAKEN INTO
5	ACCOUNT UNDER FAIR MARKET VALUE EXCEP-
6	TION.—
7	"(A) IN GENERAL.—In determining wheth-
8	er paragraph (2)(B) applies to any transfer by
9	a person described in clause (ii) or (iii) of sub-
10	paragraph (C), there shall not be taken into
11	account—
12	"(i) except as provided in regulations,
13	any obligation of a person described in
14	subparagraph (C), and
15	"(ii) to the extent provided in regula-
16	tions, any obligation which is guaranteed
17	by a person described in subparagraph (C).
18	"(B) Treatment of Principal Pay-
19	MENTS ON OBLIGATION.—Principal payments
20	by the trust on any obligation referred to in
21	subparagraph (A) shall be taken into account
22	on and after the date of the payment in deter-
23	mining the portion of the trust attributable to
24	the property transferred.

1	"(C) Persons described.—The persons
2	described in this subparagraph are—
3	"(i) the trust,
4	"(ii) any grantor, owner, or bene-
5	ficiary of the trust, and
6	"(iii) any person who is related (with-
7	in the meaning of section 143(i)(2)(B) to
8	any grantor, owner, or beneficiary of the
9	trust.
10	"(4) Special rules applicable to foreign
11	GRANTOR WHO LATER BECOMES A UNITED STATES
12	PERSON.—
13	"(A) IN GENERAL.—If a nonresident alien
14	individual has a residency starting date within
15	5 years after directly or indirectly transferring
16	property to a foreign trust, this section and sec-
17	tion 6048 shall be applied as if such individual
18	transferred to such trust on the residency start-
19	ing date an amount equal to the portion of such
20	trust attributable to the property transferred by
21	such individual to such trust in such transfer.
22	"(B) Treatment of undistributed in-
23	COME.—For purposes of this section, undistrib-
24	uted net income for periods before such individ-
25	ual's residency starting date shall be taken into

1	account in determining the portion of the trust
2	which is attributable to property transferred by
3	such individual to such trust but shall not oth-
4	erwise be taken into account.
5	"(C) RESIDENCY STARTING DATE.—For
6	purposes of this paragraph, an individual's resi-
7	dency starting date is the residency starting
8	date determined under section 7701(b)(2)(A).
9	"(5) Outbound trust migrations.—If—
10	"(A) an individual who is a citizen or resi-
11	dent of the United States transferred property
12	to a trust which was not a foreign trust, and
13	"(B) such trust becomes a foreign trust
14	while such individual is alive, then this section
15	and section 6048 shall be applied as if such in-
16	dividual transferred to such trust on the date
17	such trust becomes a foreign trust an amount
18	equal to the portion of such trust attributable
19	to the property previously transferred by such
20	individual to such trust. A rule similar to the
21	rule of paragraph (4)(B) shall apply for pur-
22	poses of this paragraph.
23	"(b) Trusts Acquiring United States Bene-

24 FICIARIES.—If—

1	"(1) subsection (a) applies to a trust for the
2	transferor's taxable year, and
3	"(2) subsection (a) would have applied to the
4	trust for his immediately preceding taxable year but
5	for the fact that for such preceding taxable year
6	there was no United States beneficiary for any por-
7	tion of the trust,
8	then, for purposes of this chapter, the transferor shall be
9	treated as having income for the taxable year (in addition
10	to his other income for such year) equal to the undistrib-
11	uted net income (at the close of such immediately preced-
12	ing taxable year) attributable to the portion of the trust
13	referred to in subsection (a).
14	"(c) Trusts Treated as Having a United
15	STATES BENEFICIARY.—
16	"(1) In general.—For purposes of this sec-
17	tion, a trust shall be treated as having a United
18	States beneficiary for the taxable year unless—
19	"(A) under the terms of the trust, no part
20	of the income or corpus of the trust may be
21	paid or accumulated during the taxable year to
22	or for the benefit of a United States person,
23	and
24	"(B) if the trust were terminated at any
25	time during the taxable year, no part of the in-

1	come or corpus of such trust could be paid to
2	or for the benefit of a United States person.
3	"(2) Attribution of Ownership.—For pur-
4	poses of paragraph (1), an amount shall be treated
5	as paid or accumulated to or for the benefit of a
6	United States person if such amount is paid to or
7	accumulated for a foreign corporation, foreign part-
8	nership, or foreign trust or estate, and—
9	"(A) in the case of a foreign corporation,
10	such corporation is a controlled foreign corpora-
11	tion,
12	"(B) in the case of a foreign partnership,
13	a United States person is a partner of such
14	partnership, or
15	"(C) in the case of a foreign trust or es-
16	tate, such trust or estate has a United States
17	beneficiary (within the meaning of paragraph
18	(1)).
19	"(3) CERTAIN UNITED STATES BENEFICIARIES
20	DISREGARDED.—A beneficiary shall not be treated
21	as a United States person in applying this section
22	with respect to any transfer of property to foreign
23	trust if such beneficiary first became a United
24	States person more than 5 years after the date of
25	such transfer.

- 1 "(d) Regulations.—The Secretary shall prescribe
- 2 such regulations as may be necessary or appropriate to
- 3 carry out the purposes of this section.
- 4 "SEC. 162. LIMITATION ON CHARITABLE DEDUCTION.
- 5 "In computing the deduction allowable under section
- 6 142(c) to a trust, no amount otherwise allowable under
- 7 section 142(c) as a deduction shall be allowed as a deduc-
- 8 tion with respect to income of the taxable year which is
- 9 allocable to unrelated business income for such year.
- 10 "SEC. 163. INCOME OF AN ESTATE OR TRUST IN CASE OF DI-
- 11 **VORCE, ETC.**
- 12 "(a) Inclusion in Gross Income of Wife.—There
- 13 shall be included in the gross income of a wife who is di-
- 14 vorced or legally separated under a decree of divorce or
- 15 of separate maintenance (or who is separated from her
- 16 husband under a written separation agreement) the
- 17 amount of the income of any trust which such wife is enti-
- 18 tled to receive and which, except for this section, would
- 19 be includible in the gross income of her husband, and such
- 20 amount shall not, despite any other provision of this sub-
- 21 title, be includible in the gross income of such husband.
- 22 This subsection shall not apply to that part of any such
- 23 income of the trust which the terms of the decree, written
- 24 separation agreement, or trust instrument fix, in terms
- 25 of an amount of money or a portion of such income, as

- 1 a sum which is payable for the support of minor children
- 2 of such husband. In case such income is less than the
- 3 amount specified in the decree, agreement, or instrument,
- 4 for the purpose of applying the preceding sentence, such
- 5 income, to the extent of such sum payable for such sup-
- 6 port, shall be considered a payment for such support.
- 7 "(b) Wife Considered a Beneficiary.—For pur-
- 8 poses of computing the taxable income of the estate or
- 9 trust and the taxable income of a wife to whom subsection
- 10 (a) applies, such wife shall be considered as the bene-
- 11 ficiary.
- 12 "(c) Cross Reference.—For definitions of 'hus-
- 13 band' and 'wife', as used in this section, see section
- 14 7701(a)(17).
- 15 "SEC. 164. RECOGNITION OF GAIN ON CERTAIN TRANSFERS
- 16 TO CERTAIN FOREIGN TRUSTS AND ESTATES.
- 17 "(a) In General.—Except as provided in regula-
- 18 tions, in the case of any transfer of property by a United
- 19 States person to a foreign estate or trust, for purposes
- 20 of this subtitle, such transfer shall be treated as a sale
- 21 or exchange for an amount equal to the fair market value
- 22 of the property transferred, and the transferor shall recog-
- 23 nize as gain the excess of—
- 24 "(1) the fair market value of the property so
- 25 transferred, over

- 1 "(2) the adjusted basis (for purposes of deter-
- 2 mining gain) of such property in the hands of the
- 3 transferor.
- 4 "(b) Exception.—Subsection (a) shall not apply to
- 5 a transfer to a trust by a United States person to the
- 6 extent that any person is treated as the owner of such
- 7 trust under section 153.
- 8 "(c) Treatment of Trusts Which Become For-
- 9 EIGN TRUSTS.—If a trust which is not a foreign trust be-
- 10 comes a foreign trust, such trust shall be treated for pur-
- 11 poses of this section as having transferred, immediately
- 12 before becoming a foreign trust, all of its assets to a for-
- 13 eign trust.
- 14 "SEC. 165. TREATMENT OF FUNERAL TRUSTS.
- 15 "(a) IN GENERAL.—In the case of a qualified funeral
- 16 trust, sections 144 through 161 shall not apply, and no
- 17 deduction shall be allowed by section 142(b).
- 18 "(b) Qualified Funeral Trust.—'Qualified fu-
- 19 neral trust' means any trust (other than a foreign trust)
- 20 if—
- 21 "(1) the trust arises as a result of a contract
- 22 with a person engaged in the trade or business of
- providing funeral or burial services or property nec-
- essary to provide such services,

1	"(2) the sole purpose of the trust is to hold, in-
2	vest, and reinvest funds in the trust and to use such
3	funds solely to make payments for such services or
4	property for the benefit of the beneficiaries of the
5	trust,
6	"(3) the only beneficiaries of such trust are in-
7	dividuals with respect to whom such services or
8	property are to be provided at their death under
9	contracts described in paragraph (1),
10	"(4) the only contributions to the trust are con-
11	tributions by or for the benefit of such beneficiaries,
12	"(5) the trustee elects the application of this
13	subsection, and
14	"(6) the trust would (but for the election de-
15	scribed in paragraph (5)) be treated as owned under
16	sections 153 through 161 by the purchasers of the
17	contracts described in paragraph (1).
18	"(c) Dollar Limitation on Contributions.—
19	"(1) In general.—Any trust which accepts
20	aggregate contributions by or for the benefit of an
21	individual in excess of \$7,000 shall not be a quali-
22	fied funeral trust.
23	"(2) Related trusts.—For purposes of para-
24	graph (1), all trusts having trustees which are relat-

1	ed persons shall be treated as 1 trust. For purposes
2	of the preceding sentence, persons are related if—
3	"(A) the relationship between such persons
4	is described in section 171(a)(5), or
5	"(B) the Secretary determines that treat-
6	ing such persons as related is necessary to pre-
7	vent avoidance of the purposes of this section.
8	"(3) Inflation adjustment.—In the case of
9	any contract referred to in subsection (b)(1) which
10	is entered into during any calendar year after 1998,
11	the dollar amount referred to in paragraph (1) shall
12	be adjusted for inflation in accordance with section
13	23.
14	"(d) Application of Rate Schedule.—Section
15	140(b) shall be applied to each qualified funeral trust by
16	treating each beneficiary's interest in each such trust as
17	a separate trust.
18	"(e) Treatment of Amounts Refunded to Pur-
19	CHASER ON CANCELLATION.—No gain or loss shall be rec-
20	ognized to a purchaser of a contract described in sub-
21	section (b)(1) by reason of any payment from such trust
22	to such purchaser by reason of cancellation of such con-
23	tract. If any payment referred to in the preceding sentence
24	consists of property other than money, the basis of such
25	property in the hands of such purchaser shall be the same

1	as the trust's basis in such property immediately before
2	the payment.
3	"(f) SIMPLIFIED REPORTING.—The Secretary may
4	prescribe rules for simplified reporting of all trusts having
5	a single trustee.
6	"SEC. 166. INCOME IN RESPECT OF A DECEDENT.
7	"(a) Inclusion in Gross Income.—
8	"(1) General use.—The amount of all items
9	of gross income in respect of a decedent which are
10	not properly includible in respect of a taxable period
11	in which falls the date of his death, or a prior pe-
12	riod, shall be included in gross income, for the tax-
13	able year when received, of—
14	"(A) the estate of the decedent, if the right
15	to receive the amount is acquired by the dece-
16	dent's estate,
17	"(B) the person who, by reason of the
18	death of the decedent, acquires the right to re-
19	ceive the amount, if the right to receive the
20	amount is not acquired by the decedent's estate
21	from the decedent,
22	"(C) the person who acquires from the de-
23	cedent the right to receive the amount by be-
24	quest, devise or inheritance, if the amount is re-

1	ceived after a distribution by the decedent's es-
2	tate of such right.
3	"(2) Definition.—The Secretary shall pre-
4	scribe regulations on the treatment of income from
5	sales of rights to receive income and installment
6	sales.
7	"(b) The amount of any homeowner deduction or for-
8	eign tax credit in respect of a decedent which is not prop-
9	erly allowable to the decedent with respect to the taxable
10	period in which falls the date of his death, or a prior pe-
11	riod, shall be allowed in accordance with regulations that
12	reflect the principles of section 691(b) of the Internal Rev-
13	enue Code of 1986.
14	"Subchapter J—Definitions and Rules of
14 15	"Subchapter J—Definitions and Rules of Application
	-
	Application "Sec. 171. Definitions.
15	Application "Sec. 171. Definitions. "Sec. 172. Rules of application.
15 16	Application "Sec. 171. Definitions. "Sec. 172. Rules of application. "SEC. 171. DEFINITIONS.
15 16 17	**Sec. 171. Definitions. "Sec. 172. Rules of application. "SEC. 171. DEFINITIONS. "(a) IN GENERAL.—When used in this chapter,
15 16 17 18	**Sec. 171. Definitions. "Sec. 172. Rules of application. "SEC. 171. DEFINITIONS. "(a) IN GENERAL.—When used in this chapter, where not otherwise distinctly expressed or manifestly in-
115 116 117 118 119	**Sec. 171. Definitions. "Sec. 172. Rules of application. **SEC. 171. DEFINITIONS. **(a) In General.—When used in this chapter, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—
15 16 17 18 19 20	**Sec. 171. Definitions. "Sec. 172. Rules of application. "SEC. 171. DEFINITIONS. "(a) IN GENERAL.—When used in this chapter, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof— "(1) BUSINESS ENTITY.—The definition of
15 16 17 18 19 20 21	"Sec. 171. Definitions. "Sec. 172. Rules of application. "SEC. 171. DEFINITIONS. "(a) IN GENERAL.—When used in this chapter, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof— "(1) BUSINESS ENTITY.—The definition of 'business entity' in section 206 (relating to the business)

1	posed by section 201 and, to the extent required by
2	the context, the provisions of chapter 2.
3	"(3) Internal revenue code of 1986.—'In-
4	ternal Revenue Code of 1986' means the Internal
5	Revenue Code of 1986 as in effect immediately be-
6	fore the enactment of the Simplified USA Tax Act
7	of 1998.
8	"(4) United States' means
9	the States and the District of Columbia.
10	"(5) Related party.—'Related party'
11	means—
12	"(A) Members of a family, as defined in
13	paragraph (6)(D);
14	"(B) An individual and a business entity
15	more than 50 percent in value of which is
16	owned, directly or indirectly, by or for such in-
17	dividual (applying rules of constructive owner-
18	ship);
19	"(C) Two business entities that are eligible
20	to file a consolidated return under chapter 2;
21	"(D) A grantor and a fiduciary of any
22	trust;
23	"(E) A fiduciary of a trust and a fiduciary
24	of another trust, if the same person is a grantor
25	of both trusts:

1	"(F) A fiduciary of a trust and a bene-
2	ficiary of such trust;
3	"(G) A fiduciary of a trust and a bene-
4	ficiary of another trust, if the same person is
5	a grantor of both trusts;
6	"(H) A fiduciary of a trust and a corpora-
7	tion more than 50 percent in value of the out-
8	standing stock of which is owned, directly or in-
9	directly, by or for the trust or by or for a per-
10	son who is a grantor of the trust;
11	"(I) A person and an organization to
12	which section 251 (relating to certain edu-
13	cational and charitable organizations which are
14	exempt from tax) applies and which is con-
15	trolled directly or indirectly by such person or
16	(if such person is an individual) by members of
17	the family of such individual;
18	"(J) Two business entities if the same per-
19	sons own more than 50 percent of the value of
20	each (applying rules of constructive ownership),
21	with value measured by—
22	"(i) the value of the outstanding stock
23	in the case of a corporation,
24	"(ii) the capital interest or the profits
25	interest, whichever is greater, in the case

1	of a partnership or limited liability com-
2	pany;
3	"(K) Except in the case of a sale or ex-
4	change in satisfaction of a pecuniary bequest,
5	an executor of an estate and a beneficiary of
6	such estate.
7	"(6) Constructive ownership.—For pur-
8	poses of determining, in applying paragraph (5), the
9	ownership of a business entity—
10	"(A) Stock or other equity interest owned,
11	directly or indirectly, by or for a corporation,
12	partnership, estate, or trust shall be considered
13	as being owned proportionately by or for its
14	shareholders, partners, or beneficiaries;
15	"(B) An individual shall be considered as
16	owning the stock or other equity interest owned,
17	directly or indirectly, by or for his family;
18	"(C) An individual owning (otherwise than
19	by the application of subparagraph (B)) any
20	stock in a corporation or other equity interest
21	in another form of business entity shall be con-
22	sidered as owning the stock owned, directly or
23	indirectly, by or for his partner;
24	"(D) The family of an individual shall in-
25	clude only his brothers and sisters (whether by

1	the whole or half blood), spouse, ancestors, and
2	lineal descendants; and
3	"(E) Stock or other equity interest con-
4	structively owned by a person by reason of the
5	application of subparagraph (A) shall, for the
6	purpose of applying subparagraph (A), (B), or
7	(C), be treated as actually owned by such per-
8	son, but stock or other equity interest construc-
9	tively owned by an individual by reason of the
10	application of subparagraph (B) or (C) shall
11	not be treated as owned by him for the purpose
12	of again applying either of such paragraphs in
13	order to make another the constructive owner of
14	such stock or equity interest.
15	"(6) Earned income.—
16	"(A) In GENERAL.—'Earned income'
17	means—
18	"(i) wages, salaries, tips, and other
19	employee compensation, plus
20	"(ii) the amount of the taxpayer's net
21	earnings from self-employment for the tax-
22	able year (within the meaning of section
23	1402(a)).
24	"(B) Special rules.—For purposes of
25	subparagraph (A)—

1	"(i) the earned income of an individ-
2	ual shall be computed without regard to
3	any community property laws,
4	"(ii) no amount received as a pension
5	or annuity shall be taken into account,
6	"(iii) no income of nonresident alien
7	individuals not connected with United
8	States business shall be taken into ac-
9	count, and
10	"(iv) no amount received for services
11	provided by an individual while the individ-
12	ual is an inmate at a penal institution shall
13	be taken into account.
14	"(b) Terms Defined in Chapter 1.—If a term
15	that is used but not defined in this chapter or in section
16	7701 is defined in chapter 2, the definition in chapter 2
17	shall apply except if manifestly incompatible with the in-
18	tent of the provision in which the term is used.
19	"SEC. 172. RULES OF APPLICATION.
20	"(a) Definitions.—Any definition included in this
21	chapter shall apply for all purposes of this chapter
22	unless—
23	"(1) such definition is limited to the purposes
24	of a particular chapter, section, or subsection, or

1	"(2) the definition clearly would not be applica-
2	ble in a particular context.
3	"(b) Interpretations Consistent With Inter-
4	NAL REVENUE CODE OF 1986.—Terms not defined in this
5	chapter or elsewhere in this title, but defined in the Inter-
6	nal Revenue Code of 1986, shall be interpreted in a man-
7	ner consistent with the Internal Revenue Code of 1986,
8	except to the extent such interpretation would be incon-
9	sistent with the principles and purposes of this chapter."
10	(c) Exemption From Prohibited Transaction
11	Tax.—Section 4975(g) of the Code is amended by—
12	(1) striking "or" at the end of paragraph (2),
13	(2) deleting the period at the end of paragraph
14	(3) and inserting "; or",
15	(3) and inserting the following new paragraph
16	(4):
17	"(4) to a Roth IRA in the case of a loan to or
18	equity investment in a controlled business entity as
19	permitted by section 30(f))."

1 TITLE III—SIMPLIFIED USA TAX

FOR BUSINESSES

- 3 SEC. 301. REPEAL OF CORPORATE INCOME TAX; NEW TAX
- 4 PAID BY CORPORATIONS AND OTHER BUSI-
- 5 NESSES.
- 6 (a) IN GENERAL.—Chapter 2 of the Internal Reve-
- 7 nue Code is renumbered chapter 3 and following new
- 8 chapter is inserted after chapter 1:

9 "CHAPTER 2—SIMPLIFIED USA TAX FOR

10 BUSINESSES

- "Subchapter A. Imposition of tax.
- "Subchapter B. Basic rules for business tax.
- "Subchapter C. Capital contributions, mergers, acquisitions, and distributions.
- "Subchapter D. Accounting methods.
- "Subchapter E. Land and rental property.
- "Subchapter F. Insurance and financial products.
- "Subchapter G. Financial intermediation and financial institutions.
- "Subchapter H. Tax-exempt organizations.
- "Subchapter I. Cooperatives.
- "Subchapter J. Sourcing rules.
- "Subchapter K. Business conducted in a possession.
- "Subchapter L. Payroll tax credit.
- "Subchapter M. Import tax.
- "Subchapter N. Transition rules.
- "Subchapter O. Rules for administration, consolidated returns.
- "Subchapter P. Definitions and rules of applications.

11 "Subchapter A—Imposition of Tax

- 12 **"SEC. 201. TAX IMPOSED.**
- 13 "(a) Taxable Business Activity.—A tax is im-
- 14 posed on the sale of goods and services in the United
- 15 States by a business entity. The amount of the tax equals
- 16 the amount by which—

[&]quot;Sec. 201. Tax imposed.

1	"(1) the business tax exceeds,
2	"(2) the payroll tax credit.
3	"(b) Business Tax Imposed.—
4	"(1) In general.—The 'business tax' imposed
5	on a business entity that sells or leases property or
6	sells services in the United States equals the sum
7	of—
8	"(A) 8 percent of the portion of the gross
9	profits of the business entity for the taxable
10	year that does not exceed \$150,000, and
11	"(B) 12 percent of such portion of the
12	gross profits of the business entity for the tax-
13	able year that exceeds \$150,000.
14	"(2) Limitation on application of Bene-
15	FITS OF GRADUATED RATE SCHEDULE.—The Sec-
16	retary shall prescribe rules under which the gross
17	profits of business entities under common control
18	are aggregated for purposes of applying the benefit
19	of the lower rate described in subparagraph (A) of
20	paragraph (1). Such rules shall be similar to rules
21	applicable under sections 1551 and 1561 of the In-
22	ternal Revenue Code of 1986.
23	"(c) Payroll Tax Credit.—The 'payroll tax credit'
24	is a credit for the social security, railroad retirement and
25	hospital insurance taxes paid by an employer, as deter-

- 1 mined in accordance with subchapter L (sections 281
- 2 through 283).
- 3 "(d) IMPORT TAX.—For rules relating to the import
- 4 tax imposed by this chapter, see subchapter M (sections
- 5 286 through 288).

6 "Subchapter B—Basic Rules for Business Tax

- "Sec. 202. Gross profits.
- "Sec. 203. Taxable receipts.
- "Sec. 204. Deductible amounts.
- "Sec. 205. Cost of business purchases.
- "Sec. 206. Business entity and business activity.
- "Sec. 207. Loss carryover deduction.

7 "SEC. 202. GROSS PROFITS.

- 8 "'Gross profits' means for a taxable year of a busi-
- 9 ness entity the amount by which—
- "(1) the taxable receipts of the business entity
- 11 for the taxable year exceed,
- 12 "(2) the deductible amounts for the business
- entity for the taxable year.

14 "SEC. 203. TAXABLE RECEIPTS.

- 15 "(a) In General.—'Taxable receipts' means all re-
- 16 ceipts from the sale of property, use of property, and per-
- 17 formance of services in the United States.
- 18 "(b) Games of Chance.—Amounts received for
- 19 playing games of chance by business entities engaging in
- 20 the activity of providing such games shall be treated as
- 21 receipts from the sale of property or services.

1	"(c) In-Kind Receipts.—The taxable receipts at-
2	tributable to the receipt of property, use of property or
3	services in whole or partial exchange for property, use of
4	property or services equal the fair market value of the
5	services or property received.
6	"(d) Taxes.—Taxable receipts do not include any ex-
7	cise tax, sales tax, custom duty, or other separately stated
8	levy imposed by a Federal, State, or local government re-
9	ceived by a business entity in connection with the sale of
10	property or services or the use of property.
11	"(e) Financial Receipts.—
12	"(1) IN GENERAL.—Excepts as provided in sub-
13	chapter G (relating to financial intermediation and
14	financial institutions), taxable receipts do not in-
15	clude financial receipts.
16	"(2) Financial receipts.—'Financial re-
17	ceipts' include—
18	"(A) interest,
19	"(B) dividends and other distributions by a
20	business entity,
21	"(C) proceeds from the sale of stock, other
22	ownership interests in business entities, or
23	other financial instruments (as defined in sec-
24	tion $242(b)(3)$,
25	"(D) proceeds from life insurance policies,

1	"(E) proceeds from annuities,
2	"(F) proceeds from currency hedging or
3	exchanges, and
4	"(G) proceeds from other financial trans-
5	actions.
6	"(f) Cross References.—
7	"(1) Financial intermediation.—See sub-
8	chapters F and G for rules relating to financial
9	intermediation.
10	"(2) Exports, sales in the united
11	STATES.—See subchapter J for the exclusion from
12	gross receipts for export sales and for rules on sales
13	of property and services in the United States.
14	"(3) Land.—See subchapter E for rules relat-
15	ing to certain sales of land.
16	"(4) Insurance proceeds.—See section 237
17	for rules on the inclusion of certain insurance pro-
18	ceeds in taxable receipts.
19	"SEC. 204. DEDUCTIBLE AMOUNTS.
20	"(a) In General.—'Deductible amounts' for a busi-
21	ness entity in a taxable year include—
22	"(1) the cost of business purchases in the tax-
23	able year (as determined under section 205),
24	"(2) such entity's loss carryover deduction (as
25	determined under section 207), and

1	"(3) the transition basis deduction (as deter-
2	mined under section 290).
3	"(b) Financial Intermediation.—See subchapters
4	F and G for special rules for business entities engaging
5	in financial intermediation.
6	"SEC. 205. COST OF BUSINESS PURCHASES.
7	"(a) Business Purchases.—
8	"(1) In general.—'Business purchases' means
9	the acquisition of—
10	"(A) property,
11	"(B) the use of property, or
12	"(C) services
13	in the United States for use in a business activity.
14	"(2) Examples.—Business purchases include
15	(without limitation) the—
16	"(A) purchase or rental of real property,
17	"(B) purchase or rental of capital equip-
18	ment,
19	"(C) purchase of supplies and inventory,
20	"(D) purchase of services from independ-
21	ent contractors,
22	"(E) purchase of financial intermediation
23	services (as determined in accordance with sec-
24	tion 236).

1	"(F) purchase of a business loss policy (as
2	determined in accordance with section 237),
3	and
4	"(G) imports for use in a business activity.
5	"(3) Exclusions.—Business purchases do not
6	include—
7	"(A) payments for use of money or capital,
8	such as interest or dividends (except to the ex-
9	tent that a portion so paid is a fee for financial
10	intermediation services),
11	"(B) premiums for life insurance,
12	"(C) the acquisition of savings assets or
13	other financial instruments (as defined in sec-
14	tion $242(b)(3)$).
15	"(D) property acquired outside the United
16	States (but such property shall be taken into
17	account as an import if imported),
18	"(E) services performed outside the United
19	States (unless treated as imported into the
20	United States),
21	"(F) compensation expenses for an individ-
22	ual (other than amounts paid to an individual
23	in his capacity as a business entity), or
24	"(G) taxes (except as provided in sub-
25	section $(b)(2)$ relating to product taxes).

1	"(4) Compensation expenses.—'Compensa-
2	tion expenses' means—
3	"(A) wages, salaries or other cash payable
4	for services,
5	"(B) any taxes imposed on the recipient
6	that are withheld by the business entity,
7	"(C) the cost of property purchased to pro-
8	vide employees with compensation (other than
9	property incidental to the provision of fringe
10	benefits that are excluded from income under
11	the individual tax),
12	"(D) the cost of fringe benefits which are
13	includible in an employee's, partner's, or propri-
14	etor's income under the Simplified USA Income
15	Tax (or are excluded solely because they con-
16	stitute employee savings), including (without
17	limitation)—
18	"(i) contributions to retirement and
19	severance benefit plans,
20	"(ii) premiums for the cost of life,
21	health, accident, disability and other insur-
22	ance policies for which the service provider,
23	members of his family, or persons des-
24	ignated by him or members of his family
25	are the beneficiaries,

1	"(iii) rental of parking spaces or park-
2	ing fees (unless the parking space is used
3	for a vehicle that is regularly used in a
4	business activity);
5	"(iv) employer paid educational bene-
6	fits;
7	"(v) employer paid housing (other
8	than housing provided for the convenience
9	of the employer); and
10	"(vi) employer paid meals (other than
11	meals provided for the convenience of the
12	employer).
13	"(b) Cost of Business Purchases.—
14	"(1) In general.—The 'cost of a business
15	purchase' is the amount paid or to be paid for the
16	business purchase.
17	"(2) Taxes.—
18	"(A) In general.—The 'cost of business
19	purchases' includes any product taxes paid with
20	respect to the property or services purchased.
21	"(B) Product Tax.—'Product tax' means
22	any excise tax, sales or use tax, custom duty, or
23	other separately stated levy imposed by a Fed-
24	eral, State, or local government on the produc-
25	tion, severance or consumption of property or

1	on the provision of services, whether or not sep-
2	arately stated, and including any such taxes
3	that are technically imposed on the seller of
4	property or services.
5	"(C) Taxes not product taxes.—Prod-
6	uct taxes do not include—
7	"(i) the import tax,
8	"(ii) state and local property taxes,
9	"(iii) franchise or income taxes,
10	"(iv) payroll taxes and self-employ-
11	ment taxes, or
12	"(v) the business tax.
13	"(3) Imports.—In the case of an import by a
14	business entity, the cost of the import is the import
15	price for purposes of the import tax. The import tax
16	is not part of the cost of the import.
17	"(c) Property and Services Acquired for
18	Property.—If a business entity receives property or serv-
19	ices from a business entity in whole or partial exchange
20	for property or services, the property or services acquired
21	shall be treated as if they were purchased for an amount
22	equal to the fair market value of the services or property
23	received. For purposes of this section, property includes
24	stock and other equity interests in business other than
25	stock or an equity interest in the business entity acquiring

- 1 the property or services. See section 210(b) for rules on
- 2 property or services received in exchange for an equity in-
- 3 terest in the recipient.
- 4 "(d) Gambling Payments.—In the case of a busi-
- 5 ness involving gambling, lotteries, or other games of
- 6 chance, business purchases include amounts paid to win-
- 7 ners.
- 8 "(e) Savings Assets.—'Savings assets' means
- 9 stocks, bonds, securities, certificates of deposits, invest-
- 10 ments in partnerships and limited liability companies,
- 11 shares of mutual funds, life insurance policies, annuities,
- 12 and other similar savings or investment assets.
- "(f) Cross References.
- 14 "(1) Financial intermediation and insur-
- 15 ANCE.—For rules relating to fees for financial inter-
- mediation services and insurance, see subchapter F.
- 17 "(2) Land.—For special rules relating to the
- acquisition of land, see subchapter E.
- 19 "(3) Rental real estate.—For special rules
- 20 relating to the rental of real estate previously occu-
- 21 pied by an owner of the real estate, see section 232.
- 22 "(4) Outside the united states.—For spe-
- cial rules relating to services performed outside the
- United States but used inside the United States and
- international services, see subchapter J.

1 "SEC. 206. BUSINESS ENTITY AND BUSINESS ACTIVITY.

2	"(a) Business Entity.—For purposes of the busi-
3	ness tax, 'business entity' means any corporation, unincor-
4	porated association, partnership, limited liability company,
5	proprietorship, independent contractor, individual, or any
6	other person engaging in business activity in the United
7	States. An individual shall be considered a business entity
8	only with respect to the individual's business activities.
9	"(b) Business Activity.—'Business activity' means
10	the sale of property or services, the leasing of property,
11	the development of property or services for subsequent
12	sale or use in producing property or services for subse-
13	quent sale. 'Business activity' does not include casual or
14	occasional sales of property used by an individual (other
15	than in a business activity), such as the sale by an individ-
16	ual of a vehicle used by the individual.
17	"(c) Exception for Certain Employees.—
18	"(1) In general.—'Business activity' does not
19	include—
20	"(A) the performance of services by an em-
21	ployee for an employer that is a business entity
22	with respect to the activity in which the em-
23	ployee is engaged, or
24	"(B) the performance of regular domestic
25	household services (including babysitting,
26	housecleaning, and lawn cutting) by an em-

1	ployee of an employer that is an individual or
2	family.
3	"(2) Employee defined.—For purposes of
4	this subsection, 'employee' includes an individual
5	partner who provides services to a partnership or an
6	individual member who provides services to a limited
7	liability company, or a proprietor with respect to
8	compensation for services from his proprietorship.
9	"SEC. 207. LOSS CARRYOVER DEDUCTION.—
10	"(a) Deduction.—The 'loss carryover deduction' for
11	a taxable year is the lesser of—
12	"(1) the business entity's gross profits for the
13	taxable year (determined without the loss carryover
14	deduction), or
15	"(2) the amount of the loss carryover to the
16	taxable year.
17	"(b) Loss Carryover.—
18	"(1) General rule.—A loss for any taxable
19	year shall be a loss carryover to each of the 215 tax-
20	able years following the taxable year of the loss.
21	"(2) Loss carryovers to a taxable year.—
22	The loss carryover to a taxable year is the sum of
23	the loss carryovers from all prior taxable years be-
24	ginning on or after January 1, 1999, that can be
25	carried over to the taxable year.

1	"(3) Reduction of loss carryovers as a
2	RESULT OF THE DEDUCTION.—A business entity's
3	loss carryovers shall be reduced each year by the
4	amount of the loss carryover deduction for the year.
5	Loss carryovers shall be reduced in the order that
6	they arose.
7	"(c) Loss for Taxable Year.—A business entity's
8	loss (if any) for the taxable year equals the excess (if any)
9	of—
10	"(1) the sum of—
11	"(A) the cost of business purchases for the
12	taxable year, and
13	"(B) the transition basis adjustment for
14	the taxable year, over
15	"(2) taxable receipts for the taxable year.
16	"(d) Special Rules.—
17	"(1) Consolidated returns.—In the case of
18	a consolidated return, the loss for a taxable year
19	shall be determined on a consolidated group basis.
20	In the case of a deconsolidation, the loss carryovers
21	from the consolidated group shall be allocated in ac-
22	cordance with rules to be prescribed by the Sec-
23	retary.
24	"(2) Loss carryovers of acquired busi-
25	NESS ENTITY.—

"(A) In general.—If a business entity acquires another business entity in a transaction that is considered the acquisition of a business entity and the two entities file a consolidated return or if two business entities merge, the loss carryovers will survive and can be applied against the taxable receipts attributable to the business activities carried on (or in the case of a merger formerly carried on) by either entity.

"(B) ASSET ACQUISITION.—If a business entity acquires all or substantially all of the assets of another entity in a transaction that is considered an asset acquisition rather than the acquisition of a business entity, the acquirer will be treated as if it acquired the loss carryovers of the selling entity. For purposes of this rule, the assets of a business entity include ownership interests in other business entities.

"(C) Substantially all.—For purposes of this paragraph 'substantially all' means more than 80 percent of the fair market value of a business entity's net assets. Under rules prescribed by the Secretary, the parties to a transaction may elect to treat acquisitions in excess

of 70 percent of the fair market value of a business entity's net assets as acquisitions of 'substantially all' of a business entity's net assets.

4 "Subchapter C—Capital Contributions,

5 Mergers, Acquisitions, and Distributions

"Sec. 210. Contributions to a business entity.

6 "SEC. 210. CONTRIBUTIONS TO A BUSINESS ENTITY.

- 7 "(a) By Business Entity.—
- "(1) Cash.—If a business entity contributes cash to a business entity of which it is or becomes a partial or full owner, the amount contributed is not a deductible amount to the contributor or a taxable receipt to the recipient.
 - "(2) Property or services.—If a business entity contributes property or services to a business entity of which it is or becomes a partial or full owner, the transaction will not result in taxable receipts to the contributor or a deduction for a business purchase for the recipient and will not constitute a sale resulting in taxable receipts to the contributor.
- 21 "(b) By Individual.—

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[&]quot;Sec. 211. Distributions of property.

[&]quot;Sec. 212. Asset acquisitions.

[&]quot;Sec. 213. Mergers and stock acquisitions.

[&]quot;Sec. 214. Spin-offs, split-off, etc.

[&]quot;Sec. 215. Allocation of certain tax attributes.

1	"(1) Cash.—If an individual contributes cash
2	to a business entity, the cash received is not a tax-
3	able receipt.

"(2) NEW PROPERTY.—If an individual contributes to a business entity property that the individual purchased for the business entity but which was not used by any person after its purchase, the property shall be considered purchased by such business entity from the person from which the individual purchased the property.

"(3) Personal use property.—

"(A) IN GENERAL.—If an individual contributes personal use property to a business entity in which the individual has an ownership interest or for which the individual receives an ownership interest, the business entity shall not be permitted to deduct the value of the property received as a business expense. The business entity will have a tax basis in the contributed property equal to the contributor's basis.

"(B) Personal use property "Personal use property" means any property used by an individual at any time other than in a business activity.

"(4) Services.—If an individual contributes services to a business entity in which the individual has an ownership interest or receives an ownership interest, the business entity shall not be permitted to deduct the value of the services received (or the value of the equity interest provided to the services provider).

8 "SEC. 211. DISTRIBUTIONS OF PROPERTY.

- 9 "(a) Distributions Other Than to Control-
- 10 LING BUSINESS.—If a business entity distributes all or a
- 11 portion of its assets to its owners (other than a controlling
- 12 business entity), the business entity will be treated as if
- 13 it sold the assets to its owners at fair market value. The
- 14 fair market value will be determined by the distributing
- 15 corporation and those determinations, unless unreason-
- 16 able, will be binding on the recipients.
- 17 "(b) Distributions to a Controlling Busi-
- 18 NESS.—If a business entity distributes all or a portion of
- 19 its assets to a controlling business, the controlling busi-
- 20 ness will assume the distributing entity's tax attributes
- 21 with respect to the assets and neither entity will have tax-
- 22 able receipts or a deduction as a result of the transaction.
- 23 "(c) Distribution of Personal Use Prop-
- 24 ERTY.—If personal use property is distributed to the indi-
- 25 vidual who contributed the personal use property to a busi-

- 1 ness entity, the fair market value of the property for pur-
- 2 poses of paragraph (a) shall equal the basis of the prop-
- 3 erty plus any enhancement in value of the property attrib-
- 4 utable to business purchases with respect to the property.
- 5 "(d) Controlling Business Entity.—A business
- 6 entity is a 'controlling business entity' with respect to an-
- 7 other business entity if it owns directly or indirectly more
- 8 than 50 percent of the profits or capital interest in the
- 9 other business entity.
- 10 "(e) Application of This Section.—This section
- 11 applies to both liquidating and nonliquidating distribu-
- 12 tions. Property shall be treated as distributed if the prop-
- 13 erty is used for a nonbusiness purpose (as defined in sec-
- 14 tion 232) for more than an insubstantial period of time
- 15 during a taxable year. See section 232 for rules relating
- 16 to certain rental property.

17 "SEC. 212. ASSET ACQUISITIONS.

- 18 "(a) In General.—If a business entity transfers
- 19 some or all of its assets, the consideration received for
- 20 such assets shall be allocated among the assets transferred
- 21 in the same manner as was required by section 1060 of
- 22 the Internal Revenue Code of 1986. If the transferee and
- 23 transferor agree in writing on the allocation of any consid-
- 24 eration, or as to the fair market value of any of the assets,
- 25 such agreement shall be binding on both the transferor

- 1 and transferee unless the Secretary determines that such
- 2 allocation (or fair market value) is not appropriate.
- 3 "(b) Tax Consequences.—The tax consequences of
- 4 an asset acquisition shall be determined in accordance
- 5 with the rules of this chapter and shall be dependent upon
- 6 allocations made under subsection (a). In general, consid-
- 7 eration allocable to savings assets, such as stock in an-
- 8 other business entity, would not be included in taxable re-
- 9 ceipts of the transferor and would not be a business pur-
- 10 chase of the purchaser, but consideration allocable to the
- 11 sale of tangible property and intangible property (other
- 12 than savings assets) will constitute taxable receipts of the
- 13 seller and a business purchase of the purchaser.
- 14 "(c) Election To Treat Asset Acquisition as a
- 15 Stock Acquisition.—In the case of the sale of substan-
- 16 tially all of the assets of a business entity or substantially
- 17 all of the assets of a line of business or a separately stand-
- 18 ing business of a business entity, the transferee and trans-
- 19 feror can jointly elect to treat the acquisition as if it were
- 20 an acquisition of the stock of a business entity holding
- 21 the assets so transferred. In such case, the rules of section
- 22 213 shall apply.
- 23 "(d) Authority To Require Allocation Agree-
- 24 MENT AND NOTICE TO THE SECRETARY.—If the Sec-
- 25 retary determines that certain types of asset acquisitions

1	have significant possibilities of tax avoidance, the Sec-
2	retary may require—
3	"(1) parties to such types of acquisitions to
4	enter into agreements allocating consideration,
5	"(2) parties to acquisitions involving certain
6	kinds of assets to enter into agreements allocating
7	part of the consideration to those assets, or
8	"(3) parties to certain acquisitions to report in-
9	formation to the Secretary.
10	"(e) Asset Acquisition Rules Do Not Apply if
11	Consideration Includes Equity in Purchaser.—
12	"(1) In general.—If a business entity issues
13	its own equity or equity in a subsidiary or other con-
14	trolled entity as part of the consideration for the
15	transfer of assets to it, the transaction shall not be
16	treated as an asset acquisition and the rules of sec-
17	tion 13 shall apply.
18	"(2) Equity.—For purposes of this subsection,
19	equity means—
20	"(A) stock, in the case of a corporation,
21	"(B) partnership or similar interest, in the
22	case of a partnership or limited liability com-
23	pany, and
24	"(C) an ownership interest or interest in
25	profits in the case of any other business entity.

1 "SEC. 213. MERGERS AND STOCK ACQUISITIONS.

- 2 "(a) Mergers.—A merger of one business entity
- 3 into another or two businesses entities into a third busi-
- 4 ness entity or any other similar transaction shall have no
- 5 direct consequences under the business tax. The surviving
- 6 entity shall assume the tax attributes of the merged cor-
- 7 porations, including any loss carryovers and credit
- 8 carryovers.
- 9 "(b) STOCK ACQUISITION.—The acquisition of all or
- 10 substantially all of the ownership interest in one business
- 11 entity either for cash or in exchange for ownership in the
- 12 acquiring entity or an entity controlled by the acquired
- 13 entity shall have no direct consequences under the busi-
- 14 ness tax.
- 15 "SEC. 214. SPIN-OFFS, SPLIT-OFFS, ETC.
- 16 "A spin-off, split-off or split-up of a business entity
- 17 shall have no direct tax consequences under the business
- 18 tax.
- 19 "SEC. 215. ALLOCATION OF CERTAIN TAX ATTRIBUTES.
- 20 "The Secretary shall prescribe rules for allocation of
- 21 loss carryovers and payroll tax credit carryovers in cases
- 22 of substantial shifts of assets from one business entity to
- 23 another business entity. Under such rules, a portion of a
- 24 business entity's carryovers may be deemed transferred
- 25 when assets are transferred.

1 "Subchapter D—Accounting Method Rules

- "Sec. 220. General accounting rules.
- "Sec. 221. Use of the cash method of accounting.
- "Sec. 222. Taxable year.
- "Sec. 223. Long-term contracts.
- "Sec. 224. Post-sale price adjustments and refunds.
- "Sec. 225. Bad debts.
- "Sec. 226. Transition rules.

2 "SEC. 220. GENERAL ACCOUNTING RULES.

- 3 "(a) In General.—Except as provided in section
- 4 221, a business entity shall use an accrual method of ac-
- 5 counting for purposes of determining the timing of rec-
- 6 ognition of taxable receipts and deduction of business pur-
- 7 chases. All business purchases shall be deducted when in-
- 8 curred (in the case of a business entity using the accrual
- 9 method of accounting) or when paid (in case of a business
- 10 entity using the cash method of accounting) without re-
- 11 gard to whether the business purchases are for or relate
- 12 to—
- 13 "(1) inventory,
- 14 "(2) assets with a useful life of more than one
- 15 year, or
- 16 "(3) property that will be used to produce other
- 17 property.
- 18 "(b) Economic Performance.—For purposes of
- 19 determining whether an amount has been incurred, the all
- 20 events test shall not be treated as met any earlier than
- 21 when economic performance with respect to such item oc-
- 22 curs.

1	"(c) Consistent Accounting Methods.—Except
2	as otherwise expressly provided in this chapter, a business
3	entity shall secure the consent of the Secretary before
4	changing the method of accounting by which it determines
5	gross profits. This provision shall not apply to changes
6	required by the adoption of the business tax.
7	"SEC. 221. USE OF THE CASH METHOD OF ACCOUNTING.
8	"(a) In General.—A business entity that was per-
9	mitted to use and used the cash method of accounting
10	under the Internal Revenue Code of 1986 shall be per-
11	mitted to continue to use the cash method of accounting.
12	"(b) New Business Entities.—A new business en-
13	tity shall be permitted to use the cash method of account-
14	ing if permitted to under regulations prescribed by the
15	Secretary.
16	"(c) Change or Expansion of Business.—Sub-
17	section (a) shall cease to apply to a business entity that
18	changes or expands its business such that under regula-
19	tions prescribed by the Secretary it is no longer eligible
20	to use the cash method of accounting.
21	"(d) Regulations.—
22	"(1) Use of Cash Method.—The Secretary
23	shall prescribe regulations defining which business
24	entities may use the cash method of accounting. In

general, those regulations shall be consistent with

1	the rules under sections 447 and 448 of the Internal
2	Revenue Code of 1986, except that all corporations
3	shall be treated as C corporations were treated
4	under those sections. The regulations shall not re-
5	quire a business entity described in subsection (a) to
6	convert to the accrual method prior to January 1,
7	2000.
8	"(2) Change in accounting method.—The
9	Secretary shall prescribe regulations to prevent dou-
10	ble counting of taxable receipts and deductible ex-
11	penses in the case of a change in accounting method.
12	"SEC. 222. TAXABLE YEAR.
13	"(a) Computation of Gross Profits.—Gross
14	profits shall be computed on the basis of a business enti-
15	ty's taxable year.
16	"(b) Taxable Year.—"Taxable year' means—
17	"(1) the taxpayer's annual accounting period, if
18	it is a calendar year or a fiscal year;
19	"(2) the calendar year, if subsection (g) applies;
20	or
21	"(3) the period for which the return is made if

the return is made for a period of less than 12

months.

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1	"(c) Annual Accounting Period.—'Annual ac-
2	counting period' means the annual period on the basis of
3	which the business entity regularly keeps its books.
4	"(d) CALENDAR YEAR.—'Calendar year' means a pe-
5	riod of 12 months ending on December 31.
6	"(e) Fiscal Year.—'Fiscal year' means a period of
7	12 months ending on the last day of any month other than
8	December. In the case of any business entity that has
9	made the election provided by subsection (f), the term
10	means the annual period (varying from 52 to 53 weeks)
11	so elected.
12	"(f) Election of 52–53 Week Year.—
13	"(1) General Rule.—A business entity which,
14	in keeping its books, regularly computes its income
15	or profits on a basis of an annual period which var-
16	ies from 52 to 53 weeks and ends always on the
17	same day of the week and ends always—
18	"(A) on whatever date such same day of
19	the week last occurs in a calendar month, or
20	"(B) on whatever date such same day of
21	the week falls which is nearest to the last day
22	of a calendar month,
23	may elect to compute its gross profits on the basis
24	of such annual period.

"(2) REGULATIONS.—The Secretary shall pre-1 2 scribe such regulations as he deems necessary for 3 the application of this subsection, including regula-4 tions relating to the application of effective dates to 5 taxpayers using a 52–53 week year. 6 "(g) Calendar Year Required.— 7 "(1) No accounting period.—A business en-8 tity's taxable year shall be the calendar year if the 9 business entity does not have an annual accounting 10 period or has an annual accounting period that does 11 not qualify as a fiscal year. "(2) New Business entity.—The taxable 12 13 year of a business entity that begins business activ-14 ity after December 31, 1998, shall be the calendar 15 year (or a 52–53 week fiscal year ending in Decem-16 ber) unless the business entity can demonstrate a 17 business reason for selecting an accounting period 18 other than the calendar year. 19 "(h) Transition Rule for Business Entities 20 WITH A FISCAL YEAR.— "(1) IN GENERAL.—A business entity with a 21 22 taxable year that is not the calendar year shall have 23 a short taxable year ending on December 31, 1998, 24 and a subsequent taxable year beginning on January

1, 1999, and ending on the day immediately preced-

1	ing the beginning of the business entity's next fiscal
2	year.
3	"(2) Business entities with 52–53 week
4	YEAR ENDING IN DECEMBER.—
5	"(A) IN GENERAL.—If a business entity
6	has a $52-53$ week taxable year (under the In-
7	ternal Revenue Code of 1986) that ends in De-
8	cember 1998, it may elect to begin its first tax-
9	able year for the business tax on the first day
10	immediately following the last day of such tax-
11	able year.
12	"(B) No election.—If a business entity
13	that has a 52–53 week taxable year that ends
14	in December 1998, does not make the election
15	under subparagraph (A) or is prohibited from
16	making such election by subparagraph (C), the
17	business entity's taxable year under the Inter-
18	nal Revenue Code of 1986 that would end in
19	December 1998 shall end on December 31,
20	1998.
21	"(C) Anti-abuse rule.—Subparagraph
22	(A) shall not apply to any taxpayer that enters
23	into business transactions in 1998 following the
24	scheduled end of its fiscal year with business
25	entities that are not subject to the business tax

1	at the time of such transactions if such trans-
2	actions deviate from the normal course of busi-
3	ness in order to achieve some tax benefit.
4	"SEC. 223. LONG-TERM CONTRACTS.
5	"(a) In General.—In the case of a long-term
6	contract—
7	"(1) Contractor expenses.—The contractor
8	shall be entitled to deduct its business purchases
9	when paid or incurred.
10	"(2) Contractor receipts.—The contractor
11	shall recognize taxable receipts—
12	"(A) in the case of a project in which the
13	acquirer has no ownership interest in the
14	project until delivery—
15	"(i) upon delivery of the project, in
16	the case of an accrual basis contractor, or
17	"(ii) upon the later of delivery of the
18	project or the receipt of payment, in the
19	case of cash-basis contractor.
20	"(B) in the case of a project in which the
21	acquirer obtains an ownership interest as the
22	project is constructed—
23	"(i) when the contractor has the right
24	to payments, in the case of an accrual
25	basis contractor, or

1	"(ii) upon the later of when the con-
2	tractor receives the cash or has the right
3	to payments, in the case of a cash basis
4	contractor.
5	"(3) Acquirer expenses.—The acquirer that
6	is a business entity shall be entitled to deduct its
7	costs of the business purchase—
8	"(A) in the case of a cash-basis acquirer,
9	at such time as a cash basis contractor would
10	be required to treat the amounts paid as tax-
11	able receipts, or
12	"(B) in the case of an accrual-basis
13	acquirer, at such time as an accrual basis con-
14	tractor would be required to treat the amounts
15	paid or due as taxable receipts.
16	"(b) Right to Payments.—
17	"(1) In general.—A contractor shall be treat-
18	ed as having a right to payments with respect to a
19	project at any time to the extent that the contractor
20	would not be required to return payments received
21	(or would be entitled to collect payments not yet re-
22	ceived) if the project were terminated at such time
23	by the contractor.
24	"(2) Contractual provisions.—If a long-
25	term contract includes a procedure for paying the

1	contractor as work is completed (for example, by
2	reason of a draw down from a trust account), the
3	contractual provisions shall generally govern when a
4	contractor has a right to payment.
5	"(3) Percentage completion method of
6	ACCOUNTING.—If a long-term contract does not in
7	clude a mechanism for paying the contractor as
8	work is completed, the percentage-of-completion
9	method of accounting shall be used to determine the
10	timing of taxable receipts of the contractor and busi
11	ness purchases of the acquirer.
12	"(c) Long-Term Contract.—
13	"(1) In General.—'Long-term contract
14	means—
15	"(A) any contract that covers service of
16	production through parts of two different cal
17	endar years if the contract includes a forma
18	deposit and draw-down mechanism, and
19	"(B) any contract for the manufacture
20	building, installation, or construction of prop
21	erty if such contract is not completed within the
22	taxable year of the contractor in which such
23	contract is entered into.
24	"(2) EXCEPTION —A contract for the manufac

ture of property shall not be treated as a long-term

1	contract unless such contract involves the manufac-
2	ture of—
3	"(A) any unique item of a type which is
4	not normally included in the finished goods in-
5	ventory of the taxpayer, or
6	"(B) any item which normally requires
7	more than 12 calendar months to complete.
8	"(d) Consistency.—The Secretary may require
9	business entities to file statements containing such infor-
10	mation with respect to long-term contracts as the Sec-
11	retary may prescribe to ensure consistency in reporting.
12	"(e) Foreign Contracts.—This section shall not
13	be construed to permit a deduction for a business purchase
14	for the cost of property produced outside the United
15	States pursuant to a long-term contract at any time prior
16	to the import of such property into the United States.
17	"SEC. 224. POST-SALE PRICE ADJUSTMENTS AND REFUNDS.
18	"(a) RECEIPT OF PRICE ADJUSTMENT.—In the case
19	of a post-sale price adjustment attributable to a business
20	purchase which was taken into account in computing gross
21	profits for a prior taxable year, the amount of such adjust-
22	ment shall be treated as a reduction or increase, as the
23	case may be, in the cost of business purchases for the tax-
24	able year in which the adjustment is made or incurred.

- 1 "(b) Issuance of Price Adjustment.—In the case
- 2 of a post-sale price adjustment attributable to a sale the
- 3 receipts from which were taken into account in determin-
- 4 ing taxable receipts for a prior taxable year, the amount
- 5 of such adjustment shall be treated as a reduction or in-
- 6 crease, as the case may be, in taxable receipts for the tax-
- 7 able year in which the adjustment is made or incurred.
- 8 "(c) Post-Sale Price Adjustment.—'Post-sale
- 9 price adjustment' means a refund, rebate, or other price
- 10 allowance attributable to a sale of property or services or
- 11 an upward adjustment in price that was not previously
- 12 taken into account under the business entity's method of
- 13 accounting.
- 14 "SEC. 225. BAD DEBTS.
- 15 "(a) Seller.—If an amount owed to an accrual
- 16 basis business entity for property or services sold—
- 17 "(1) was taken into account as a taxable receipt
- in a prior taxable year, and
- 19 "(2) becomes wholly or partially uncollectible
- during the taxable year, then the seller shall treat
- 21 the amount as a reduction in taxable receipts for the
- taxable year in which it becomes wholly or partially
- 23 uncollectible.
- 24 "(b) Notice Requirement.—No reduction shall be
- 25 allowed under subsection (a) unless the seller notifies the

- 1 purchaser of the amount which the seller has treated as
- 2 wholly or partially uncollectible.
- 3 "(c) Subsequent Collection.—If an amount
- 4 which was treated as uncollectible under subsection (a) is
- 5 subsequently collected, it shall be treated as a taxable re-
- 6 ceipt when collected.
- 7 "(d) Purchaser.—If a purchaser receives notice
- 8 under subsection (b) from a seller and the purchaser has
- 9 treated the amount labeled uncollectible as a business pur-
- 10 chase in a prior taxable year, then the purchaser shall
- 11 treat such amount as a reduction in the cost of business
- 12 purchases in the taxable year to which the notice relates.
- 13 If the purchaser subsequently repays such amount, the re-
- 14 payment shall constitute the cost of a business purchase.
- 15 "SEC. 226. TRANSITION RULES.
- 16 "(a) No Double Deductions.—A business entity
- 17 shall not be entitled to treat as a 'cost of business pur-
- 18 chase' any amount that the business entity deducted in
- 19 computing taxable income under the income tax in effect
- 20 prior the effective date of the business tax.
- 21 "(b) No Double Inclusion.—A business entity
- 22 shall not be required to include in taxable receipts any
- 23 receipt that the business entity took into account in com-
- 24 puting taxable income under the income tax in effect prior
- 25 to the effect date of the business tax.

1	"(c) No Loss of Deduction.—An expense which—
2	"(1) a business entity would have been able to
3	deduct as a cost of a business purchase in an ac-
4	counting period before the effective date of the busi-
5	ness tax if the business tax had been in effect in
6	such period, and
7	"(2) the business entity would have been able to
8	deduct as an expense in computing taxable income
9	in a period after the business tax is effective if the
10	income tax had continued in effect,
11	shall be treated as a cost of a business purchase incurred
12	or paid at the time that it would have been paid or in-
13	curred under the income tax if the income tax had contin-
14	ued in effect. This subsection shall not apply to any
15	amount which is to be taken into account under sub-
16	chapter N (relating to amortization of transition basis, in-
17	ventory costs, and safe harbor leases), any amounts which
18	would have been deducted under the income tax through
19	loss carryover deductions, or any deductions deferred by
20	the uniform capitalization rules under section 263A of the
21	Internal Revenue Code of 1986.
22	"(d) ALL TAXABLE RECEIPTS TAXED.—A receipt
23	which—
24	"(1) a business entity would have been required
25	to treat as a taxable receipt in an accounting period

1	before the effective date of the business tax if the
2	business tax had been in effect in such period, and
3	"(2) the business entity would have been re-
4	quired to include in gross income in a period after
5	the business tax is effective if the income tax had
6	continued in effect
7	shall be treated as a taxable receipt at the time that it
8	would have been included in income if the income tax had
9	continued in effect.
10	"Subchapter E—Land and rental property
	"Sec. 230. No deduction for land purchased for nonbusiness use. "Sec. 231. Taxable receipts for land held for nonbusiness use. "Sec. 232. Certain rental property.
11	"SEC. 230. NO DEDUCTION FOR LAND PURCHASED FOR
1112	"SEC. 230. NO DEDUCTION FOR LAND PURCHASED FOR NONBUSINESS USE.
12	NONBUSINESS USE.
12 13	Nonbusiness use. "(a) In General.—The acquisition of unimproved
12 13 14 15	NONBUSINESS USE. "(a) IN GENERAL.—The acquisition of unimproved land shall not constitute a business purchase if the unim-
12 13 14 15	NONBUSINESS USE. "(a) In General.—The acquisition of unimproved land shall not constitute a business purchase if the unimproved land is not acquired to be used in a business activ-
12 13 14 15 16	NONBUSINESS USE. "(a) IN GENERAL.—The acquisition of unimproved land shall not constitute a business purchase if the unimproved land is not acquired to be used in a business activity or if the land is acquired for—
12 13 14 15 16 17	NONBUSINESS USE. "(a) IN GENERAL.—The acquisition of unimproved land shall not constitute a business purchase if the unimproved land is not acquired to be used in a business activity or if the land is acquired for— "(1) speculation,
12 13 14 15 16 17	NONBUSINESS USE. "(a) IN GENERAL.—The acquisition of unimproved land shall not constitute a business purchase if the unimproved land is not acquired to be used in a business activity or if the land is acquired for— "(1) speculation, "(2) development (including subdivision), or
12 13 14 15 16 17 18 19	"(a) In General.—The acquisition of unimproved land shall not constitute a business purchase if the unimproved land is not acquired to be used in a business activity or if the land is acquired for— "(1) speculation, "(2) development (including subdivision), or "(3) temporary leasing or other use not com-
12 13 14 15 16 17 18 19 20	NONBUSINESS USE. "(a) IN GENERAL.—The acquisition of unimproved land shall not constitute a business purchase if the unimproved land is not acquired to be used in a business activity or if the land is acquired for— "(1) speculation, "(2) development (including subdivision), or "(3) temporary leasing or other use not commensurate with the value of the land,

- 1 "(b) Future Use in Business Activity.—Unim-
- 2 proved land will not be considered held for 'indefinite fu-
- 3 ture use in a business activity' if promptly upon acquisi-
- 4 tion, the purchaser or the lessee begins construction of im-
- 5 provements on the land (other than improvements, such
- 6 as paving or sewage lines, intended for indefinite future
- 7 development) that will be used in a business activity. Such
- 8 improvement must be commensurate with the value of the
- 9 land.
- 10 "(c) Unimproved land'
- 11 means—
- "(1) land with no buildings on it,
- "(2) land with improvements if the value of the
- improvements is relatively small in comparison to
- 15 the value of the land and it is anticipated that the
- improvements will be demolished and not used,
- 17 "(3) land in excess of the amount reasonably
- 18 needed for the buildings located on it.
- 19 "(d) Conversion to Business Use.—If the acqui-
- 20 sition of land is not treated as a business purchase by rea-
- 21 son of subsection (a) and the land is subsequently used
- 22 in a manner for which it could have been treated as a
- 23 business purchase, the cost of the land will be treated as
- 24 a business purchase when the improvements on the land

- 1 are placed in service (or in the case of construction for
- 2 sale, substantially completed and advertised for sale).
- 3 "SEC. 231. TAXABLE RECEIPTS FROM SALE OF LAND HELD
- 4 FOR NONBUSINESS USE.
- 5 "(a) Tax Basis.—A business entity shall have a tax
- 6 basis in land equal to the cost of the land if such cost
- 7 is not deductible by reason of section 230(a) and the land
- 8 has not been converted to business use for purposes of
- 9 section 230(d).
- 10 "(b) Taxable Receipts of a Land Sale.—The
- 11 taxable receipts from the sale of land (or portion thereof)
- 12 in which a business entity has a tax basis by reason of
- 13 subsection (a) shall be the amount by which the proceeds
- 14 exceed the basis of such land (or portion thereof).
- 15 "SEC. 232. CERTAIN RENTAL PROPERTY.
- 16 "(a) In General.—Except as provided in subsection
- 17 (b), the activity of rental of real estate is a business activ-
- 18 ity to which the business tax applies.
- 19 "(b) Not Rental Property.—Subsection (a) shall
- 20 not apply to property described in section 111(b)(1) (relat-
- 21 ing to property owned by individuals and used for at least
- 22 14 days for a nonbusiness purpose and rented for no more
- 23 than 14 days during the taxable year).
- 24 "(c) Rental Property Becomes Nonrental
- 25 Property.—If property which is considered rental prop-

- 1 erty for purposes of subsection (a) in one taxable year
- 2 ceases to be rental property (by reason of subsection (b))
- 3 in the following taxable year, the property (and any associ-
- 4 ated debt) shall be treated as distributed by the business
- 5 entity to its owners. Section 211(a) shall apply to such
- 6 distribution.

7 "Subchapter F—Insurance and

8 Financial Products

9 "SEC. 235. GENERAL RULES.

- 10 "(a) Taxable Receipts.—Except in the case of a
- 11 financial intermediation business, taxable receipts do not
- 12 include financial receipts (as defined in section 203(e)(2)).
- 13 "(b) Business Purchases.—Except in the case of
- 14 a financial intermediation business, business purchases do
- 15 not include the cost of financial instruments (as defined
- 16 in section 242(b)(3)) or payments for use of money or cap-
- 17 ital, other than fees for financial intermediation services.
- 18 "SEC. 236. FEES FOR FINANCIAL INTERMEDIATION SERV-
- 19 **ICES.**
- 20 "(a) Business Purchase.—Business purchases in-
- 21 clude explicit fees and implicit fees for financial intermedi-
- 22 ation services (except to the extent that such fees are for
- 23 services treated as performed outside the United States

[&]quot;Sec. 235. General rules.

[&]quot;Sec. 236. Fees for financial intermediation services.

[&]quot;Sec. 237. Deductible insurance premiums.

[&]quot;Sec. 238. Nondeductible insurance premiums.

[&]quot;Sec. 239. Certain implicit fees for financial intermediate services.

1	and not imported into the United States or for services
2	treated as exported.).
3	"(b) Financial Intermediation Services.—The
4	definition of 'financial intermediation service' in section
5	241 applies for purposes of this section.
6	"(c) Explicit Fees.—
7	"(1) In general.—'Explicit fees for financial
8	intermediation services' means separately stated fees
9	for services provided by a business entity in the fi-
10	nancial intermediation business. Explicit fees do not
11	include fees for use of money or capital.
12	"(2) Examples.—Explicit fees for financial
13	intermediation services include (without limita-
14	tion)—
15	"(A) separately listed maintenance and
16	service charges of providers of financial inter-
17	mediation services,
18	"(B) loan documentation fees,
19	"(C) brokerage fees,
20	"(D) loan origination fees,
21	"(E) underwriting fees,
22	"(F) trustees' fees, and
23	"(G) fees for credit checks.
24	"(3) Exclusions.—Explicit fees for financial
25	intermediation services do not include prepaid inter-

1	est and other fees for use of money or capital even
2	if such fees are separately stated or are labeled as
3	service fees.
4	"(d) Implicit Fees.—
5	"(1) Implicit fees attributable to bor-
6	ROWING.—
7	"(A) In General.—Implicit fees attrib-
8	utable to borrowing from banks and other fi-
9	nancial institutions shall include the portion of
10	interest payments that the Secretary designates
11	as constituting service fees.
12	"(B) Timing.—Implicit fees determined
13	under this paragraph shall not be deductible in
14	any taxable year prior to the taxable year in
15	which the interest is paid. If the amount of the
16	interest to which implicit fees relate was de-
17	ducted as original issue discount under the In-
18	ternal Revenue Code of 1986, the implicit fees
19	with respect to such interest shall not constitute
20	a deductible business purchase.
21	"(C) Designation by Secretary.—
22	"(i) Estimate of differential.—
23	The Secretary shall estimate for each cal-
24	endar year the difference between the cost
25	of funds for banks and the rates of interest

1	(including discount points) charged to the
2	most credit-worthy depositors of banks.
3	The determinations shall be made sepa-
4	rately for—
5	"(I) loans with terms of not more
6	than 3 years,
7	"(II) loans with terms of over 3
8	but not over 9 years, and
9	"(III) loans with terms of over 9
10	years.
11	"(ii) Designation of Implicit
12	FEES.—The Secretary shall designate the
13	differences determined under clause (i) as
14	the portion of interest expense on loans
15	from banks and other financial institutions
16	that constitutes an implicit fee for term
17	loans originated during the following cal-
18	endar year for the respective periods listed
19	in subclauses (I) through (III) of clause
20	(i). The difference determined for loans de-
21	scribed in subclause (I) of clause (i) shall
22	apply to determine the implicit fee portion
23	of interest on demand loans outstanding
24	during the following calendar year.

1	"(iii) Historical determination.—
2	The Secretary shall make an historical de-
3	termination in accordance with the prin-
4	ciples of this subparagraph to designate
5	the portion of interest on term loans made
6	before January 1, 1998, that will con-
7	stitute implicit fees.
8	"(2) Implicit fees for other financial
9	INTERMEDIATION ACTIVITY.—Implicit fees for finan-
10	cial intermediation services include the portion of the
11	fees or other charges paid to a provider of financial
12	intermediation services (other than lending) as such
13	provider designates in accordance with section 39.
14	"SEC. 237. DEDUCTIBLE INSURANCE PREMIUMS.
15	"(a) In General.—The cost of insurance premiums
16	on business loss policies that insure risks in the United
17	States constitute costs of business purchases. Proceeds
18	from such policies constitute taxable receipts.
19	"(b) Business Loss Policy.—A 'business loss pol-
20	icy' is an insurance policy—
21	"(1) owned by a business entity,
22	"(2) the beneficiary of which is the business en-
23	tity or another business entity doing business with
24	the owner of the policy,

1	"(3) that has no inside buildup or other savings
2	component,
3	"(4) that covers losses on a loss incurred or
4	claims made basis during the term of the policy,
5	"(5) that has a term of not more than 2 years,
6	"(6) that is not a direct or indirect form of
7	compensation, and
8	"(7) that covers direct losses of the business,
9	such as—
10	"(A) damage to or theft of property used
11	in business activity,
12	"(B) tort claims against the business,
13	"(C) loss of use of business premises or
14	services,
15	"(D) malpractice, or
16	"(E) alleged or actual breach of fiduciary
17	obligations.
18	"SEC. 238. NONDEDUCTIBLE INSURANCE PREMIUMS.
19	"(a) Nondeductibility.—The cost of insurance
20	policies that are not business loss policies are not deduct-
21	ible costs of business purchases.
22	"(b) Proceeds of Nondeductible Policies.—In-
23	surance proceeds from policies described in subsection (a)
24	do not constitute taxable receipts.

1	"(c) Application of This Section to Certain
2	INSURANCE.—This section shall apply to life insurance
3	policies.
4	"SEC. 239. CERTAIN IMPLICIT FEES FOR FINANCIAL INTER-
5	MEDIATION SERVICES.
6	"(a) Deductibility of Fees.—If a financial inter-
7	mediation business (as defined in section 241(b)) elects
8	to determine implicit fees for financial intermediation
9	services pursuant to this section and notify its business
10	customers of their share of the implicit fees in accordance
11	with this section, a business entity which receives such no-
12	tice may treat the amount reported in the notice as an
13	implicit fee for financial intermediation services in the cal-
14	endar year to which such notice relates.
15	"(b) Allocation and Reporting.—
16	"(1) In general.—A financial intermediation
17	business may—
18	"(A) allocate fees received for services for
19	which no separately stated fees (or implicit fees
20	for borrowing determined under section
21	236(d)(1)) are charged among recipients of
22	such services on a reasonable and consistent
23	basis, and
24	"(B) report to each recipient not later
25	than February 15th of each year the amount so

1	allocated to it with respect to the immediately
2	preceding calendar year.
3	"(2) Maximum fees allocated.—The maxi-
4	mum amount that may be allocated by a financial
5	intermediation business for a calendar is the excess
6	of—
7	"(A) the gross profits of the financial
8	intermediation business for the calendar year
9	(as reasonably estimated by the financial inter-
10	mediation business), over
11	"(B) the explicit fees for financial inter-
12	mediation services received by the financial
13	intermediation business.
14	"(3) Reasonable allocation.—An allocation
15	will not be considered reasonable unless it takes into
16	account and allocates fees to—
17	"(A) both services provided to business en-
18	tities and services provided to individuals (other
19	than in a business capacity), and
20	"(B) both persons who receive money from
21	the financial intermediation business and per-
22	sons who pay money to the financial intermedi-
23	ation business (even though amounts allocated
24	to the former do not constitute implicit fees).

1	"(4) Regulations.—The Secretary shall pre-
2	scribe regulations relating to the allocations under
3	this subsection, including regulations addressing—
4	"(A) rules for timing of deductions of im-
5	plicit fees paid by fiscal year recipients,
6	"(B) subsequent year adjustments if a fi-
7	nancial intermediation business allocates too
8	much in a calendar year,
9	"(C) rules for advance approval from the
10	Secretary for allocation procedures, and
11	"(D) safe-harbor alternatives to the alloca-
12	tion procedures described in this subsection.
13	"(c) Not Applicable to Lending Services.—
14	This section shall not apply to lending services.
15	"Subchapter G—Financial Intermediation
16	and Financial Institutions
	"Sec. 241. Activities constituting a financial intermediation business. "Sec. 242. General rule for taxation. "Sec. 243. Special rule for banks. "Sec. 244. Insurance companies. "Sec. 245. Financial pass-through entities. "Sec. 246. Financial intermediation by other businesses.
17	"SEC. 241. ACTIVITIES CONSTITUTING A FINANCIAL INTER-
18	MEDIATION BUSINESS.
19	"(a) Financial Intermediation Business.—The
20	providing of financial intermediation services shall be con-
21	sidered a business activity. The gross profit of a business

1	determined by taking into account the rules of this sub-
2	chapter.
3	"(b) Separate Business Activity.—The provision
4	of financial intermediation services for unrelated persons
5	shall be considered a separate business activity and a busi-
6	ness shall be considered a separate entity with respect to
7	such activity. An entity engaging in such business is re-
8	ferred to in this chapter as a 'financial intermediation
9	business'.
10	"(c) Financial Intermediation by a Business.—
11	Section 246 shall apply to a business that provides finan-
12	cial intermediation services for itself and related parties
13	but generally does not provide such services for unrelated
14	parties.
15	"(d) Definitions.—
16	"(1) Financial intermediation services.—
17	'Financial intermediation services' include—
18	"(A) lending services,
19	"(B) insurance services,
20	"(C) market-making and dealer services,
21	and
22	"(D) any other service provided as busi-
23	ness activity in which a person acts as an inter-
24	mediary in—

1	"(i) the transfer of property, services,
2	or financial assets, liabilities, risks or in-
3	struments (or income or expense derived
4	therefrom) between two or more persons,
5	or
6	"(ii) the pooling of economic risk
7	among other persons
8	and derives all or a portion of such person's
9	gross receipts from streams of income or ex-
10	pense, discounts, or other financial flows associ-
11	ated with the matter with respect to which such
12	person is acting as an intermediary.
13	"(2) Lending Services.—'Lending services'
14	means the regular making of loans and providing
15	credit to, or taking deposits from customers, but
16	does not include an installment or delayed payment
17	arrangement provided by a seller of property or serv-
18	ices under which additional charges or fees are im-
19	posed by the seller for the late payment.
20	"(3) Market-making or dealer services.—
21	'Market-making or dealer services' means services
22	provided by a person who—
23	"(A) regularly purchases financial instru-
24	ments from or sells financial instruments to

1	customers in the ordinary course of a trade or
2	business,
3	"(B) regularly offers to enter into, assume,
4	offset, assign, or otherwise terminate positions
5	in financial instruments with customers in the
6	ordinary course of a trade or business.
7	"SEC. 242. GENERAL RULE FOR TAXATION.
8	"(a) In General.—In the case of a financial inter-
9	mediation business, gross profits shall be computed by—
10	"(1) substituting financial receipts for taxable
11	receipts, and
12	"(2) including financial expenses as business
13	purchases.
14	"(b) Definitions.—
15	"(1) Financial receipts.—'Financial re-
16	ceipts' means all receipts other than amounts re-
17	ceived as contributions to capital.
18	"(2) Financial expenses.—'Financial ex-
19	penses' include—
20	"(A) payments for principal and interest
21	that is properly allocable to the provision of fi-
22	nancial intermediation services,
23	"(B) the cost of and payments under fi-
24	nancial instruments (other than financial in-
25	struments in the person subject to the tax im-

1	posed under this chapter and any person relat-
2	ed to such person),
3	"(C) claims and cash surrender values paid
4	in connection with insurance or reinsurance
5	services, and
6	"(D) amounts paid for reinsurance.
7	"(3) Financial instrument.—'Financial in-
8	strument' means any—
9	"(A) share of stock in a corporation,
10	"(B) equity ownership in any widely held
11	or publicly traded partnership, trust, or other
12	business entity,
13	"(C) note, bond, debenture, or other evi-
14	dence of indebtedness,
15	"(D) interest rate, currency, or equity no-
16	tional principal contract,
17	"(E) evidence or interest in, or a derivative
18	financial instrument in, any financial instru-
19	ment described in subparagraph (A), (B), (C),
20	or (D), or any currency, including any option,
21	forward contract, short position, and any simi-
22	lar financial instrument in such a financial in-
23	strument or currency, and
24	"(F) a position which—

1	"(i) is not a financial instrument de-
2	scribed in subparagraph (A), (B), (C), (D)
3	or (E),
4	"(ii) is a hedge with respect to such
5	a financial instrument, and
6	"(iii) is clearly identified in the deal-
7	er's records as being described in this sub-
8	paragraph before the close of the day on
9	which it was acquired or entered into.
10	"(c) International Matters.—For purposes of
11	this section in the case of a financial intermediation busi-
12	ness with activity in and outside the United States—
13	"(1) Inclusion regardless of source.—
14	"(A) Financial receipts shall be determined
15	without regard to whether they are received for
16	property or service provided in or outside the
17	United States, except that financial receipts do
18	not include amounts that—
19	"(i) are not taxable receipts (as deter-
20	mined without regard to this section), but
21	"(ii) would have been taxable receipts
22	(as determined without regard to this sec-
23	tion) if they had been received for services
24	or property in the United States.

1	"(B) Financial expenses shall be deter-
2	mined without regard to whether they are re-
3	ceived for property or services acquired in or
4	outside the United States.
5	"(2) Allocation.—Under regulations pre-
6	scribed by the Secretary, gross profits (as deter-
7	mined without regard to this paragraph) shall be re-
8	duced by the amount of financial intermediation
9	gross profit attributable to financial intermediation
10	activity provided outside the United States.
11	"(3) Gross profit attributable to finan-
12	CIAL INTERMEDIATION ACTIVITY.—'Gross profits at-
13	tributable to financial intermediation activity' means
14	the excess of—
15	"(A) gross profits as determined under
16	this section (but without regard to paragraph
17	(2)), over
18	"(B) gross profits as determined without
19	regard to this subchapter.
20	"SEC. 243. SPECIAL RULES FOR BANKS.
21	"(a) In General.—In the case of a bank, gross prof-
22	its shall be determined in accordance with section 242, ex-
23	cept that—
24	"(1) Financial receipts.—Financial receipts
25	shall include only—

1	"(A) taxable receipts (as determined with-
2	out regard to this subchapter),
3	"(B) interest on loans made or acquired by
4	the bank,
5	"(C) gain on the sale of loans,
6	"(D) discount points received, and
7	"(E) any explicit fees for financial or fidu-
8	ciary services not included in subparagraphs
9	(A) through (E).
10	"(2) Financial expenses.—Financial ex-
11	penses shall include only—
12	"(A) interest paid to depositors and on
13	other funds borrowed by the bank, and
14	"(B) reasonable additions to reserves for
15	bad debts.
16	"(3) Foreclosure property.—Gross profits
17	shall properly take into account proceeds from the
18	operation or sale of foreclosure property.
19	"(b) Bank.—
20	"(1) In general.—'Bank' means a bank or
21	trust company incorporated and doing business
22	under the laws of the United States, the District of
23	Columbia, or any State, a substantial part of the
24	business of which consists of receiving deposits and
25	making loans and discounts, or of exercising fidu-

- 1 ciary powers similar to those exercised by national
- 2 banks under the authority of the Comptroller of the
- 3 Currency, and which is subject by law to supervision
- 4 and examination by State or Federal authority hav-
- 5 ing supervision over banking institutions or credit
- 6 unions. Such term includes domestic building and
- 7 loan associations and credit unions.
- 8 "(2) Other activities.—If a bank is engaged
- 9 in significant amounts of activities other than those
- described in paragraph (1), the bank shall be consid-
- ered as a separate business entity with respect to
- such other activity.

13 "SEC. 244. INSURANCE COMPANIES.

- 14 "(a) IN GENERAL.—In the case of companies provid-
- 15 ing insurance services, gross profits shall be determined
- 16 in accordance with section 242, except—
- "(1) subsection (c) of section 242 (relating to
- international operations) shall not apply, and
- 19 "(2) the rules of subchapter J (sourcing rules)
- shall apply to determine financial receipts and finan-
- cial expenses.
- 22 "(b) Result Inconsistent With Statutory In-
- 23 TENT.—If an insurance company determines that the ap-
- 24 plication of subsection (a) produces results inconsistent
- 25 with the territorial approach of the business tax, it may

1	apply to the Secretary for permission to apply section
2	242(c) in lieu of subsection (a).
3	"SEC. 245. FINANCIAL PASS-THROUGH ENTITIES.
4	"(a) In General.—In the case of a financial
5	pass-thru entity, gross profits shall be determined in
6	accordance with section 242, except—
7	"(1) financial receipts shall include contribu-
8	tions to capital,
9	"(2) financial expenses shall include—
10	"(A) distributions to persons holding inter-
11	ests in the pass-thru entity,
12	"(B) investments in related entities (in-
13	cluding wholly owned entities) engaging in real
14	estate investment.
15	"(b) Pass-Thru Entity.—
16	"(1) In general.—'Pass-thru entity' means a
17	business entity that is intended to serve as a con-
18	duit. The Secretary shall prescribe regulations defin-
19	ing pass-thru entity. Such term shall include—
20	"(A) entities that would qualify as regu-
21	lated investment companies under the Internal
22	Revenue Code of 1986,
23	"(B) entities that would qualify as real es-
24	tate investment trusts under the Internal Reve-
25	nue Code of 1986.

1	"(C) entities that would qualify as
2	REMICs under the Internal Revenue Code of
3	1986, and
4	"(D) partnerships whose purposes are to
5	invest the funds of the partners in financial in-
6	struments, distribute or reinvest the income
7	from such investments, and distribute or rein-
8	vest the proceeds from the sale of such instru-
9	ments.
10	"(2) Engagement in business activity.—
11	An entity will not qualify as a pass-thru entity if it
12	engages in more than an insubstantial amount of
13	rental or other business activity (other than invest-
14	ing in and selling financial instruments). The pre-
15	ceding sentence will not apply if the business entity
16	treats the business activity as engaged in by a sepa-
17	rate business entity (separately subject to tax under
18	this chapter).
19	"SEC. 246. FINANCIAL INTERMEDIATION BY OTHER BUSI-
20	NESSES.
21	"(a) In General.—If a business entity that is not
22	regularly in the business of providing financial intermedi-
23	ation services to unrelated parties engages in significant
24	financial intermediation activity, its gross profits shall be
25	increased by its gross profits from financial intermediation

1	activity (determined as if such activity were activity of a
2	pass-thru entity that paid all costs of such financial inter-
3	mediation activity including—
4	"(1) compensation for persons engaging in such
5	activity,
6	"(2) equipment involved in such activity, and
7	"(3) office space for persons involved in such
8	activity).
9	"(b) Proxy.—A business entity to which subsection
10	(a) applies will be treated as satisfying the requirements
11	of that subsection if it increases its gross receipts by the
12	portion of employee compensation properly allocable to the
13	provision of financial intermediation services.
14	"(c) Significant Financial Intermediation.—A
15	business will be considered as engaging in substantial fi-
16	nancial intermediation if—
17	"(1) more than 5 percent of the compensation
18	paid by the business to its employees is for employ-
19	ees whose primary activity is the management of the
20	business's investments in financial instruments, or
21	"(2) at all times during the taxable year and
22	the immediately preceding full taxable year, more
23	than 10 percent of its assets are financial instru-
24	ments other than—

1	"(A) equity interests in business entities in
2	which it holds more than 50 percent in value of
3	the outstanding equity,
4	"(B) equity interests in joint ventures in
5	which the company is actively participating,
6	"(C) purchase money loans to its cus-
7	tomers, and
8	"(D) business loans and equity invest-
9	ments that serve a direct business purpose.
10	"Subchapter H—Tax-Exempt Organizations
	(C) - 071 F
	"Sec. 251. Exemption for governmental entities. "Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity.
11	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity.
11 12	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity.
	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity. "Sec. 251. EXEMPTION FOR GOVERNMENTAL ENTITIES.
12 13	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity. "SEC. 251. EXEMPTION FOR GOVERNMENTAL ENTITIES. "(a) STATES.—Except as provided in section 252, a
12 13	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity. "Sec. 251. EXEMPTION FOR GOVERNMENTAL ENTITIES. "(a) STATES.—Except as provided in section 252, a state, political subdivision thereof and the District of Co-
12 13 14	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity. "Sec. 251. EXEMPTION FOR GOVERNMENTAL ENTITIES. "(a) STATES.—Except as provided in section 252, a state, political subdivision thereof and the District of Columbia shall be exempt from taxation under this chapter
12 13 14 15	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity. "SEC. 251. EXEMPTION FOR GOVERNMENTAL ENTITIES. "(a) STATES.—Except as provided in section 252, a state, political subdivision thereof and the District of Columbia shall be exempt from taxation under this chapter on any gross profits derived from the exercise of any es-
12 13 14 15	"Sec. 252. Taxable activity of governmental entities. "Sec. 253. Tax-exempt organizations. "Sec. 254. Special rules for (c)(3) organizations. "Sec. 255. Tax on unrelated business activity. "Sec. 256. Unrelated business activity. "SEC. 251. EXEMPTION FOR GOVERNMENTAL ENTITIES. "(a) STATES.—Except as provided in section 252, a state, political subdivision thereof and the District of Columbia shall be exempt from taxation under this chapter on any gross profits derived from the exercise of any essential governmental function.

20 session.

1	"CTO	050	TIANZADI I	A COURT TOWN	$\mathbf{O}\mathbf{E}$	COMPANIATION	TANTOT
	"SEC.	252.	TAXABLE	ACTIVITY	()H	GOVERNMENTAL	ENTI-

- TIES.
- 3 "(a) Certain Activities Taxable.—A govern-
- 4 mental entity shall be considered a business and subject
- 5 to tax on any business activity of a type frequently pro-
- 6 vided by business entities subject to tax under this chap-
- 7 ter.
- 8 "(b) Certain Activities Treated as Essential
- 9 GOVERNMENT FUNCTIONS.—Subsection (a) shall not
- 10 apply to the following activities, which shall be treated as
- 11 essential government functions:
- 12 "(1) Provision of mass transportation services.
- 13 "(2) Provision of public utility services.
- 14 "SEC. 253. TAX-EXEMPT ORGANIZATIONS.
- 15 "(a) Exemption From Taxation.—An organiza-
- 16 tion described in subsection (c) or (d) shall be exempt
- 17 from taxation under this chapter.
- 18 "(b) Tax on Unrelated Business Activity.—An
- 19 organization exempt from taxation under subsection (a)
- 20 shall be subject to tax to the extent provided in sections
- 21 255 and 256, but shall be considered a tax-exempt organi-
- 22 zation for purposes of any law that refers to tax-exempt
- 23 organizations.
- 24 "(c) List of Exempt Organizations.—The follow-
- 25 ing organizations are referred to in subsection (a):

1	"(1) Instrumentality of the united
2	STATES.—Any corporation organized under Act of
3	Congress which is an instrumentality of the United
4	States but only if such corporation—
5	"(A) is exempt from Federal income
6	taxes—
7	"(i) under such Act as amended and
8	supplemented before July 18, 1984, or
9	"(ii) under this title without regard to
10	any provision of law which is not contained
11	in this title and which is not contained in
12	a revenue Act, or
13	"(B) is described in subsection (h).
14	"(2) Title holding companies.—Corpora-
15	tions organized for the exclusive purpose of holding
16	title to property, collecting income therefrom, and
17	turning over the entire amount thereof, less ex-
18	penses, to an organization which itself is exempt
19	under this section. Rules similar to the rules of sub-
20	paragraph (G) of paragraph (25) shall apply for
21	purposes of this paragraph.
22	"(3) Charitable, educational and reli-
23	GIOUS ORGANIZATIONS.—Corporations, and any
24	community chest, fund, or foundation, organized and
25	operated exclusively for religious, charitable, sci-

entific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (g)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

"(4) Social Welfare organizations, etc.—

"(A) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

1	"(B) Subparagraph (A) shall not apply to
2	an entity unless no part of the net earnings of
3	such entity inures to the benefit of any private
4	shareholder or individual
5	"(5) Labor and agricultural organiza-
6	Tions.—Labor, agricultural, or horticultural organi-
7	zations.
8	"(6) Trade associations.—Business leagues,
9	chambers of commerce, real-estate boards, boards of
10	trade, or professional football leagues (whether or
11	not administering a pension fund for football play-
12	ers) not organized for profit and no part of the net
13	earnings of which inures to the benefit of any pri-
14	vate shareholder or individual.
15	"(7) Social clubs.—Clubs organized for
16	pleasure, recreation, and other nonprofitable pur-
17	poses, substantially all of the activities of which are
18	for such purposes and no part of the net earnings
19	of which inures to the benefit of any private share-
20	holder.
21	"(8) CERTAIN FRATERNAL SOCIETIES.—Frater-
22	nal beneficiary societies, orders, or associations—
23	"(A) operating under the lodge system or
24	for the exclusive benefit of the members of a

1	fraternity itself operating under the lodge sys-
2	tem, and
3	"(B) providing for the payment of life,
4	sick, accident, or other benefits to the members
5	of such society, order, or association or their
6	dependents.
7	"(9) VEBA'S.—Voluntary employees' bene-
8	ficiary associations providing for the payment of life,
9	sick, accident, or other benefits to the members of
10	such association or their dependents or designated
11	beneficiaries, if no part of the net earnings of such
12	association inures (other than through such pay-
13	ments) to the benefit of any private shareholder or
14	individual.
15	"(10) Other fraternal organizations.—
16	Domestic fraternal societies, orders, or associations,
17	operating under the lodge system—
18	"(A) the net earnings of which are devoted
19	exclusively to religious, charitable, scientific, lit-
20	erary, educational, and fraternal purposes, and
21	"(B) which do not provide for the payment
22	of life, sick, accident, or other benefits.
23	"(11) Local teachers' retirement
24	FUNDS.—Teachers' retirement fund associations of a
25	purely local character, if—

1	"(A) no part of their net earnings inures
2	(other than through payment of retirement ben-
3	efits) to the benefit of any private shareholder
4	or individual, and
5	"(B) the income consists solely of amounts
6	received from public taxation, amounts received
7	from assessments on the teaching salaries of
8	members, and income in respect of investments.
9	"(12) CERTAIN COOPERATIVES.—
10	"(A) Benevolent life insurance associations
11	of a purely local character, mutual ditch or irri-
12	gation companies, mutual or cooperative tele-
13	phone companies, or like organizations; but only
14	if 85 percent or more of the income consists
15	of amounts collected from members for the sole
16	purpose of meeting losses and expenses.
17	"(B) In the case of a mutual or coopera-
18	tive telephone company, subparagraph (A) shall
19	be applied without taking into account any in-
20	come received or accrued—
21	"(i) from a nonmember telephone
22	company for the performance of commu-
23	nication services which involve members of
24	the mutual or cooperative telephone com-
25	pany,

1	"(ii) from qualified pole rentals,
2	"(iii) from the sale of display listings
3	in a directory furnished to the members of
4	the mutual or cooperative telephone com-
5	pany, or
6	"(iv) from the prepayment of a loan
7	under section 306A, 306B, or 311 of the
8	Rural Electrification Act of 1936 (as in ef-
9	fect on January 1, 1987).
10	"(C) In the case of a mutual or cooperative
11	electric company, subparagraph (A) shall be ap-
12	plied without taking into account any income
13	received or accrued—
14	"(i) from qualified pole rentals, or
15	"(ii) from the prepayment of a loan
16	under section 306A, 306B, or 311 of the
17	Rural Electrification Act of 1936 (as in ef-
18	fect on January 1, 1987).
19	"(D) For purposes of this paragraph, the
20	term 'qualified pole rental' means any rental of
21	a pole (or other structure used to support
22	wires) if such pole (or other structure)—
23	"(i) is used by the telephone or elec-
24	tric company to support one or more wires
25	which are used by such company in provid-

1	ing telephone or electric services to its
2	members, and
3	"(ii) is used pursuant to the rental to
4	support one or more wires (in addition to
5	the wires described in clause (i)) for use in
6	connection with the transmission by wire
7	of electricity or of telephone or other com-
8	munications.
9	For purposes of the preceding sentence, the
10	term 'rental' includes any sale of the right to
11	use the pole (or other structure).
12	"(13) Nonprofit cemeteries.—Cemetery
13	companies owned and operated exclusively for the
14	benefit of their members or which are not operated
15	for profit; and any corporation chartered solely for
16	the purpose of the disposal of bodies by burial or
17	cremation which is not permitted by its charter to
18	engage in any business not necessarily incident to
19	that purpose and no part of the net earnings of
20	which inures to the benefit of any private share-
21	holder or individual.
22	"(14) Grandfathered mutual financial
23	INSTITUTIONS.—
24	"(A) Credit unions without capital stock
25	organized and operated for mutual purposes

1 and without profit, but only if organized before 2 July 1, 1998.

"(B) Certain corporations or associations organized before September 1, 1957, and described in subparagraphs (B) or (C) of section 501(c)(14) of the Internal Revenue Code of 1986.

"(15) Grandfathered small insurance companies.—Insurance companies organized before July 1, 1998, and described in section 501(c)(15) of the Internal Revenue Code of 1986.

"(16) Crop financing association subject to part IV of this subchapter or members thereof, for the purpose of financing the ordinary crop operations of such members or other producers, and operated in conjunction with such association. Exemption shall not be denied any such corporation because it has capital stock, if the dividend rate of such stock is fixed at not to exceed the legal rate of interest in the State of incorporation or 8 percent per annum, whichever is greater, on the value of the consideration for which the stock was issued, and if substantially all such stock (other than nonvoting preferred stock, the owners of which are not entitled or per-

1	mitted to participate, directly or indirectly, in the
2	profits of the corporation, on dissolution or other-
3	wise, beyond the fixed dividends) is owned by such
4	association, or members thereof; nor shall exemption
5	be denied any such corporation because there is ac-
6	cumulated and maintained by it a reserve required
7	by State law or a reasonable reserve for any nec-
8	essary purpose.
9	"(17) Supplemental employment benefit
10	TRUST.—
11	"(A) A trust or trusts forming part of a
12	plan providing for the payment of supplemental
13	unemployment compensation benefits, if—
14	"(i) under the plan, it is impossible,
15	at any time prior to the satisfaction of all
16	liabilities, with respect to employees under
17	the plan, for any part of the corpus or in-
18	come to be (within the taxable year or
19	thereafter) used for, or diverted to, any
20	purpose other than the providing of supple-
21	mental unemployment compensation bene-
22	fits,
23	"(ii) such benefits are payable to em-
24	ployees under a classification which is set
25	forth in the plan and which is found by the

1	Secretary not to be discriminatory in favor
2	of employees who are highly compensated
3	employees (within the meaning of section
4	414(q)), and
5	"(iii) such benefits do not discrimi-
6	nate in favor of employees who are highly
7	compensated employees (within the mean-
8	ing of section 414(q). A plan shall not be
9	considered discriminatory within the mean-
10	ing of this clause merely because the bene-
11	fits received under the plan bear a uniform
12	relationship to the total compensation, or
13	the basic or regular rate of compensation,
14	of the employees covered by the plan.
15	"(B) Rules similar to those contained in
16	subparagraphs (B) through (E) of section
17	501(c)(7) of the Internal Revenue Code of 1986
18	shall apply to subparagraph (A).
19	"(18) Grandfathered Trusts.—A trust or
20	trusts created before June 25, 1959, and described
21	in section 501(c)(18) of the Internal Revenue Code
22	of 1986.
23	"(19) CERTAIN VETERANS' ORGANIZATIONS.—
24	A post or organization of past or present members
25	of the Armed Forces of the United States, or an

1	auxiliary unit or society of, or a trust or foundation
2	for, any such post or organization—
3	"(A) organized in the United States or any
4	of its possessions,
5	"(B) at least 75 percent of the members of
6	which are past or present members of the
7	Armed Forces of the United States and sub-
8	stantially all of the other members of which are
9	individuals who are cadets or are spouses, wid-
10	ows, or widowers of past or present members of
11	the Armed Forces of the United States or of
12	cadets, and
13	"(C) no part of the net earnings of which
14	inures to the benefit of any private shareholder
15	or individual.
16	"(20) Legal service plan trusts.—An or-
17	ganization or trust created or organized in the
18	United States, the exclusive function of which is to
19	form part of a qualified group legal services plan or
20	plans.
21	"(21) BLACK LUNG ACT TRUSTS.—A trust
22	or trusts established in writing, created or organized
23	in the United States, and contributed to by any per-
24	son (except an insurance company) if—

1	"(A) the purpose of such trust or trusts is
2	exclusively—
3	"(i) to satisfy, in whole or in part, the
4	liability of such person for, or with respect
5	to, claims for compensation for disability
6	or death due to pneumoconiosis under
7	Black Lung Acts,
8	"(ii) to pay premiums for insurance
9	exclusively covering such liability,
10	"(iii) to pay administrative and other
11	incidental expenses of such trust in connec-
12	tion with the operation of the trust and the
13	processing of claims against such person
14	under Black Lung Acts, and
15	"(iv) to pay accident or health bene-
16	fits for retired miners and their spouses
17	and dependents (including administrative
18	and other incidental expenses of such trust
19	in connection therewith) or premiums for
20	insurance exclusively covering such bene-
21	fits; and
22	"(B) such trusts meets requirements simi-
23	lar to those contained in section 501(c)(21) of
24	the Internal Revenue Code of 1986.

1	"(22) Multiemployer erisa trust.—A trust
2	created or organized in the United States and estab-
3	lished in writing by the plan sponsors of multiem-
4	ployer plans if—
5	"(A) the purpose of such trust is
6	exclusively—
7	"(i) to pay any amount described in
8	section 4223(c) or (h) of the Employee Re-
9	tirement Income Security Act of 1974, and
10	"(ii) to pay reasonable and necessary
11	administrative expenses in connection with
12	the establishment and operation of the
13	trust and the processing of claims against
14	the trust,
15	"(B) no part of the assets of the trust may
16	be used for, or diverted to, any purpose other
17	than—
18	"(i) the purposes described in sub-
19	paragraph (A), or
20	"(ii) prudent investment in securities,
21	obligations, or time or demand deposits,
22	"(C) such trust meets the requirements of
23	paragraphs (2), (3), and (4) of section 4223(b),
24	4223(h), or, if applicable, section 4223(c) of the

1	Employee Retirement Income Security Act of
2	1974, and
3	"(D) the trust instrument provides that,
4	on dissolution of the trust, assets of the trust
5	may not be paid other than to plans which have
6	participated in the plan or, in the case of a
7	trust established under section 4223(h) of such
8	Act, to plans with respect to which employers
9	have participated in the fund.
10	"(23) Grandfathered veterans' insurance
11	ORGANIZATION.—Any association organized before
12	1880 more than 75 percent of the members of which
13	are present or past members of the Armed Forces
14	and a principal purpose of which is to provide insur-
15	ance and other benefits to veterans or their depend-
16	ents.
17	"(24) ERISA TRUST.—A trust described in sec-
18	tion 4049 of the Employee Retirement Income Secu-
19	rity Act of 1974 (as in effect on the date of the en-
20	actment of the Single-Employer Pension Plan
21	Amendments Act of 1986).
22	"(25) Real title holding corporation or
23	TRUST.—
24	"(A) Any corporation or trust which—

1	"(i) has no more than 35 shareholders
2	or beneficiaries,
3	"(ii) has only 1 class of stock or bene-
4	ficial interest, and
5	"(iii) is organized for the exclusive
6	purposes of—
7	"(I) acquiring real property and
8	holding title to, and collecting income
9	from, such property, and
10	"(II) remitting the entire amount
11	of income from such property (less ex-
12	penses) to 1 or more organizations de-
13	scribed in subparagraph (C) which are
14	shareholders of such corporation or
15	beneficiaries of such trust.
16	"For purposes of clause (iii), the term 'real
17	property' shall not include any interest as a
18	tenant in common (or similar interest) and
19	shall not include any indirect interest.
20	"(B) A corporation or trust shall be de-
21	scribed in subparagraph (A) without regard to
22	whether the corporation or trust is organized by
23	1 or more organizations described in subpara-
24	graph (C).

1	"(C) An organization is described in this
2	subparagraph if such organization is—
3	"(i) a qualified pension, profit shar-
4	ing, or stock bonus plan that meets the re-
5	quirements of section 401(a),
6	"(ii) a governmental plan (within the
7	meaning of section 414(d)),
8	"(iii) the United States, any State or
9	political subdivision thereof, or any agency
10	or instrumentality of any of the foregoing,
11	or
12	"(iv) any organization described in
13	paragraph (3).
14	"(D) A corporation or trust shall in no
15	event be treated as described in subparagraph
16	(A) unless such corporation or trust permits its
17	shareholders or beneficiaries—
18	"(i) to dismiss the corporation's or
19	trust's investment adviser, following rea-
20	sonable notice, upon a vote of the share-
21	holders or beneficiaries holding a majority
22	of interest in the corporation or trust, and
23	"(ii) to terminate their interest in the
24	corporation or trust by either, or both, of

1	the following alternatives, as determined by
2	the corporation or trust:
3	"(I) by selling or exchanging
4	their stock in the corporation or inter-
5	est in the trust (subject to any Fed-
6	eral or State securities law) to any or-
7	ganization described in subparagraph
8	(C) so long as the sale or exchange
9	does not increase the number of
10	shareholders or beneficiaries in such
11	corporation or trust above 35, or
12	"(II) by having their stock or in-
13	terest redeemed by the corporation or
14	trust after the shareholder or bene-
15	ficiary has provided 90 days notice to
16	such corporation or trust.
17	"(E)(i) For purposes of this paragraph—
18	"(I) a corporation which is a qualified
19	subsidiary shall not be treated as a sepa-
20	rate corporation, and
21	"(II) all assets, liabilities, and items
22	of income, deduction, and credit of a quali-
23	fied subsidiary shall be treated as assets,
24	liabilities, and such items (as the case may

1	be) of the corporation or trust described in
2	subparagraph (A).

- "(ii) For purposes of this subparagraph, the term 'qualified subsidiary' means any corporation if, at all times during the period such corporation was in existence, 100 percent of the stock of such corporation is held by the corporation or trust described in subparagraph (A).
- "(iii) For purposes of this subtitle, if any corporation which was a qualified subsidiary ceases to meet the requirements of clause (ii), such corporation shall be treated as a new corporation acquiring all of its assets (and assuming all of its liabilities) immediately before such cessation from the corporation or trust described in subparagraph (A) in exchange for its stock.
- "(F) For purposes of subparagraph (A), the term 'real property' includes any personal property which is leased under, or in connection with, a lease of real property, but only if the rent attributable to such personal property for the taxable year does not exceed 15 percent of the total rent for the taxable year attributable

1	to both the real and personal property leased
2	under, or in connection with, such lease.
3	"(G) (i) An organization shall not be treat-
4	ed as failing to be described in this paragraph
5	merely by reason of the receipt of any otherwise
6	disqualifying income which is incidentally de-
7	rived from the holding of real property.
8	"(ii) Clause (i) shall not apply if the
9	amount of gross income described in such
10	clause exceeds 10 percent of the organization's
11	gross income for the taxable year unless the or-
12	ganization establishes to the satisfaction of the
13	Secretary that the receipt of gross income de-
14	scribed in clause (i) in excess of such limitation
15	was inadvertent and reasonable steps are being
16	taken to correct the circumstances giving rise to
17	such income.
18	"(26) State established medical care in-
19	SURER.—Any membership organization if—
20	"(A) such organization is established by a
21	State exclusively to provide coverage for medical
22	care on a not-for-profit basis to individuals de-
23	scribed in subparagraph (B) through—
24	"(i) insurance issued by the organiza-
25	tion, or

1	"(ii) a health maintenance organiza-
2	tion under an arrangement with the orga-
3	nization,
4	"(B) the only individuals receiving such
5	coverage through the organization are
6	individuals—
7	"(i) who are residents of such State,
8	and
9	"(ii) who, by reason of the existence
10	or history of a medical condition—
11	"(I) are unable to acquire medi-
12	cal care coverage for such condition
13	through insurance or from a health
14	maintenance organization, or
15	"(II) are able to acquire such
16	coverage only at a rate which is sub-
17	stantially in excess of the rate for
18	such coverage through the member-
19	ship organization,
20	"(C) the composition of the membership in
21	such organization is specified by such State,
22	and
23	"(D) no part of the net earnings of the or-
24	ganization inures to the benefit of any private
25	shareholder or individual. A spouse and any

1	qualifying child) of an individual described in
2	subparagraph (B) (without regard to this sen-
3	tence) shall be treated as described in subpara-
4	graph (B).
5	"(27) Grandfathered workers compensa-
6	TION ORGANIZATION.—Any membership organiza-
7	tion established before June 1, 1996, by a State ex-
8	clusively to reimburse its members for losses arising
9	under workmen's compensation acts, and described
10	in section 501(c)(27) of the Internal Revenue Code
11	of 1986.
12	"(d) Religious and Apostolic Organizations.—
13	The following organizations are referred to in subsection
14	(a): Religious or apostolic associations or corporations, if
15	such associations or corporations have a common treasury
16	or community treasury, even if such associations or cor-
17	porations engage in business for the common benefit of
18	the members, but only if such activity is treated as unre-
19	lated business activity.
20	"(e) Cooperative Hospital Service Organiza-
21	TIONS.—For purposes of this chapter, an organization
22	shall be treated as an organization organized and operated
23	exclusively for charitable purposes, if—
24	"(1) such organization is organized and oper-

25

ated solely—

1	"(A) to perform, on a centralized basis,
2	one or more of the following services which, if
3	performed on its own behalf by a hospital which
4	is an organization described in subsection $(c)(3)$
5	and exempt from taxation under subsection (a),
6	would constitute activities in exercising or per-
7	forming the purpose or function constituting
8	the basis for its exemption: data processing,
9	purchasing (including the purchasing of insur-
10	ance on a group basis), warehousing, billing
11	and collection, food, clinical, industrial engi-
12	neering, laboratory, printing, communications,
13	record center, and personnel (including selec-
14	tion, testing, training, and education of person-
15	nel) services; and
16	"(B) to perform such services solely for
17	two or more hospitals each of which is—
18	"(i) an organization described in sub-
19	section (e)(3) which is exempt from tax-
20	ation under subsection (a),
21	"(ii) a constituent part of an organi-
22	zation described in subsection (c)(3) which
23	is exempt from taxation under subsection
24	(a) and which, if organized and operated
25	as a separate entity, would constitute an

1	organization described in subsection $(c)(3)$,
2	or
3	"(iii) owned and operated by the
4	United States, a State, the District of Co-
5	lumbia, or a possession of the United
6	States, or a political subdivision or an
7	agency or instrumentality of any of the
8	foregoing;
9	"(2) such organization is organized and oper-
10	ated on a cooperative basis and allocates or pays,
11	within 8½ months after the close of its taxable year,
12	all net earnings to patrons on the basis of services
13	performed for them; and
14	"(3) if such organization has capital stock, all
15	of such stock outstanding is owned by its patrons.
16	"For purposes of this title, any organization which, by rea-
17	son of the preceding sentence, is an organization described
18	in subsection (c)(3) and exempt from taxation under sub-
19	section (a), shall be treated as a hospital and as an organi-
20	zation referred to in section $101(b)(1)(A)(iii)$.
21	"(f) Cooperative Service Organizations of Op-
22	ERATING EDUCATIONAL ORGANIZATIONS.—For purposes
23	of this chapter, if an organization is—
24	"(1) organized and operated solely to hold,
25	commingle, and collectively invest and reinvest (in-

1	cluding arranging for and supervising the perform-
2	ance by independent contractors of investment serv-
3	ices related thereto) in stocks and securities, the
4	moneys contributed thereto by each of the members
5	of such organization, and to collect income there-
6	from and turn over the entire amount thereof, less
7	expenses, to such members,
8	"(2) organized and controlled by one or more
9	such members, and
10	"(3) comprised solely of members that are orga-
11	nizations described in clause (ii) or (iv) of section
12	101(b)(1)(A)—
13	"(A) which are exempt from taxation
14	under subsection (a), or
15	"(B) the gross profits of which are ex-
16	cluded from taxation under section 251(a),
17	then such organization shall be treated as an organization
18	organized and operated exclusively for charitable purposes. $$
19	"(g) Expenditures by Public Charities To In-
20	FLUENCE LEGISLATION.—
21	"(1) GENERAL RULE.—In the case of an orga-
22	nization to which this subsection applies, exemption
23	from taxation under subsection (a) shall be denied
24	because a substantial part of the activities of such
25	organization consists of carrying on propaganda, or

1	otherwise attempting, to influence legislation, but
2	only if such organization normally—
3	"(A) makes lobbying expenditures in ex-
4	cess of the lobbying ceiling amount for such or-
5	ganization for each taxable year, or
6	"(B) makes grass roots expenditures in ex-
7	cess of the grass roots ceiling amount for such
8	organization for each taxable year.
9	"(2) Definitions.—For purposes of this
10	subsection—
11	"(A) Lobbying expenditures.—'Lobby-
12	ing expenditures' means expenditures for the
13	purpose of influencing legislation (as defined in
14	section 4911(d)).
15	"(B) Lobbying ceiling amount.—The
16	lobbying ceiling amount for any organization
17	for any taxable year is 150 percent of the lob-
18	bying nontaxable amount for such organization
19	for such taxable year, determined under section
20	4911.
21	"(C) Grass roots expenditures.—
22	'Grass roots expenditures' means expenditures
23	for the purpose of influencing legislation (as de-
24	fined in section 4911(d) without regard to para-
25	graph (1)(B) thereof).

1	"(D) Grass roots ceiling amount.—
2	The grass roots ceiling amount for any organi-
3	zation for any taxable year is 150 percent of
4	the grass roots nontaxable amount for such or-
5	ganization for such taxable year, determined
6	under section 4911.
7	"(3) Organizations to which this sub-
8	SECTION APPLIES.—This subsection shall apply to
9	any organization which has elected (in such manner
10	and at such time as the Secretary may prescribe) to
11	have the provisions of this subsection apply to such
12	organization and which, for the taxable year which
13	includes the date the election is made, is described
14	in subsection (c)(3) and is not described in para-
15	graph (4) and is not a private foundation.
16	"(4) Disqualified organizations.—This
17	subsection does not apply to—
18	"(A) a church,
19	"(B) an integrated auxiliary of a church or
20	of a convention or association of churches, or
21	"(C) a member of an affiliated group of or-
22	ganizations (within the meaning of section
23	4911(f)(2)) if one or more members of such
24	group is described in subparagraph (A) or (B).

1	"(5) Years for which election is effec-
2	TIVE.—An election by an organization under this
3	subsection shall be effective for all taxable years of
4	such organization which—
5	"(A) end after the date the election is
6	made, and
7	"(B) begin before the date the election is
8	revoked by such organization (under regulations
9	prescribed by the Secretary).
10	"(6) No effect on certain organiza-
11	TIONS.—With respect to any organization for a tax-
12	able year for which—
13	"(A) such organization is described in
14	paragraph (5), or
15	"(B) an election under this subsection is
16	not in effect for such organization, nothing in
17	this subsection or in section 4911 shall be con-
18	strued to affect the interpretation of the phrase,
19	'no substantial part of the activities of which is
20	carrying on propaganda, or otherwise attempt-
21	ing, to influence legislation,' under subsection
22	(e)(3).
23	"(h) Government Corporations Exempt Under
24	Subsection $(c)(1)$.—For purposes of subsection $(c)(1)$,

1	the following organizations are described in this sub-
2	section:
3	"(1) The Central Liquidity Facility established
4	under title III of the Federal Credit Union Act (12 $$
5	U.S.C. 1795 et seq.).
6	"(2) The Resolution Trust Corporation estab-
7	lished under section 21A of the Federal Home Loan
8	Bank Act.
9	"(3) The Resolution Funding Corporation es-
10	tablished under section 21B of the Federal Home
11	Loan Bank Act.
12	"(i) CERTAIN EDUCATIONAL ORGANIZATIONS.—An
13	organization shall not be eligible for exemption as an edu-
14	cational organization under subsection $(c)(3)$ if a substan-
15	tial amount of its activities and funds are devoted to-
16	"(1) conducting seminars and other similar pro-
17	grams,
18	"(2) conducting research to educate Congress
19	or the general public about public policy issues,
20	"(3) producing books and pamphlets, or
21	"(4) a combination of the foregoing.
22	"SEC. 254. SPECIAL RULES FOR (c)(3) ORGANIZATIONS.
23	"(a) New Organizations Must Notify Sec-
24	RETARY.—Except as provided in subsection (c), an organi-

zation shall not be treated as an organization described 2 in section 253(c)(3)— 3 "(1) unless that it has given notice to the Sec-4 retary, in such manner as the Secretary may pre-5 scribe, that it is applying for recognition of such sta-6 tus, or "(2) for any period before giving of such notice, 7 8 if such notice is given after the time prescribed by 9 the Secretary by regulations for giving notice under 10 this subsection. 11 "(b) Presumption That Organizations Are Pri-VATE FOUNDATIONS.—Except as provided in subsection 13 (c), any organization described in section 253(c)(3) and which does not notify the Secretary, at such time and in 14 15 such manner as the Secretary may by regulations pre-16 scribe, that it is not a private foundation (as defined in 17 section 102) shall be presumed to be a private foundation. 18 "(c) Exceptions.—Subsections (a) and (b) shall not 19 apply to— "(1) organizations organized before October 10, 20 21 1969; 22 "(2) organizations which obtained recognition 23 of tax-exempt status under section 501(c)(3) of the 24 Internal Revenue Code of 1986 (in the case of sub-25 section (a) only);

1	"(3) organizations which were determined not
2	to be private foundations under the Internal Reve-
3	nue Code of 1986;
4	"(4) churches, their integrated auxiliaries, and
5	conventions and associations of churches;
6	"(5) any organization that is not a private
7	foundation and the gross receipts of which in each
8	taxable year are not more than \$25,000, or
9	"(6) such other classes of organizations which
10	the Secretary may exempt.
11	"SEC. 255. TAX ON UNRELATED BUSINESS ACTIVITY.
12	"(a) In General.—Each organization described in
13	subsection (b) shall be subject to the Simplified USA Tax
14	for businesses under section 201 on its gross profits from
15	its unrelated business activity.
16	"(b) Organizations Subject to Tax.—This sec-
17	tion shall apply to—
18	"(1) organizations exempt from the business
19	tax under section 253(a), other than instrumental-
20	ities of the United States described in section
21	253(c)(1).
22	"(2) colleges and universities which are instru-
23	mentalities of any government and corporations
24	owned by one or more such colleges or universities.

1 "SEC. 256. UNRELATED BUSINESS ACTIVITY.

2	"(a) In General.—'Unrelated business activity'
3	means any trade or business the conduct of which is not
4	substantially related (aside from the need of such organi-
5	zation for income or funds or the use it makes of the prof-
6	its derived) to the exercise or performance by such organi-
7	zation of its charitable, educational, or other purpose or
8	function constituting the basis for its exemption under
9	section 253, except that such term does not include any
10	trade or business—
11	"(1) in which substantially all the work in car-
12	rying on such trade or business is performed for the
13	organization without compensation; or
14	"(2) which is carried on, in the case of an orga-
15	nization described in section 253(c)(3) or in the case
16	of a college or university described in section 255(b),
17	by the organization primarily for the convenience of
18	its members, students, patients, officers, or employ-
19	ees, which is the selling by the organization of items
20	of work-related clothes and equipment and items
21	normally sold through vending machines, through
22	food dispensing facilities, or by snack bars, for the
23	convenience of its members at their usual places of
24	employment: or

1	"(3) which is the selling of merchandise, sub-
2	stantially all of which has been received by the orga-
3	nization as gifts or contributions.
4	"(b) Advertising, Etc., Activities.—For pur-
5	poses of this section, 'trade or business' includes any activ-
6	ity which is carried on for the production of income from
7	the sale of goods or the performance of services. For pur-
8	poses of the preceding sentence, an activity does not lose
9	identity as a trade or business merely because it is carried
10	on within a larger aggregate of similar activities or within
11	a larger complex of other endeavors which may, or may
12	not, be related to the exempt purposes of the organization.
13	Where an activity carried on for profit constitutes an un-
14	related trade or business, no part of such trade or business
15	shall be excluded from such classification merely because
16	it does not result in profit.
17	"(c) Trade or Business.—
18	"(1) Certain business activities.—An ac-
19	tivity shall not be considered a 'trade or business'
20	solely because the activity is a business activity
21	(such as certain passive rental activity) that would
22	be subject to the business tax if conducted by a busi-
23	ness entity other than a tax-exempt organization.
24	"(2) REGULATIONS.—The Secretary shall pre-

scribe regulations defining a 'trade or business.'

1	Such regulations shall be consistent with the provi-
2	sions under sections 511 through 513 of the Internal
3	Revenue Code of 1986, except to the extent such
4	provisions are inconsistent with other principles of
5	the business tax. The regulations shall include exclu-
6	sions from the definition of 'trade or business' simi-
7	lar to those contained in section 513 of the Internal
8	Revenue Code for—
9	"(A) certain bingo games,
10	"(B) certain hospital services, and
11	"(C) certain public entertainment activity
12	at fairs and expositions by an organization
13	which regularly conducts, as one of its substan-
14	tial exempt purposes, an agricultural or edu-
15	cational fair or exhibition.
16	"(3) Trade shows.—The conduct of trade
17	shows and conventions shall not be excluded from
18	the definition of trade or business.

"Subchapter I—Cooperatives

Sec. 260. Patronage dividends of cooperatives.

20 "SEC. 260. PATRONAGE DIVIDENDS OF COOPERATIVES.

"(a) Patronage Dividends Paid by Supply Co-22 operatives.—A qualified patronage dividend paid by a 23 supply cooperative to a patron shall be treated as if it is 24 a refund of a portion of the amounts paid by the patron

- 1 for goods, services, or use of capital. In general, if the
- 2 supply cooperative included the amount received from the
- 3 patron in taxable receipts, the dividend shall reduce tax-
- 4 able receipts in the year incurred. If the recipient of the
- 5 dividend is a business entity which deducted the cost of
- 6 business purchases to which the dividend related, the re-
- 7 cipient will reduce its cost of business purchases by the
- 8 amount of the dividend in the year the dividend is paid
- 9 or incurred.
- 10 "(b) Patronage Dividends Paid by Marketing
- 11 Cooperatives.—A qualified patronage dividend paid to
- 12 a patron by a marketing cooperative shall be treated as
- 13 an upward price adjustment in the amount received by the
- 14 patron for its goods marketed by the cooperative. In gen-
- 15 eral, the cooperative will increase its cost of business pur-
- 16 chases by the amount of the qualified patronage dividend
- 17 and the recipient will increase its taxable receipts by the
- 18 amount of the qualified patronage dividend.
- 19 "(c) Dividend Treatment.—Only the portion of a
- 20 patronage dividend that is not a qualified patronage divi-
- 21 dend shall be treated as a dividend under this chapter and
- 22 chapter 2.
- 23 "(d) Definitions.—
- 24 "(1) Qualified patronage dividend.—A
- 25 'qualified patronage dividend' is that part of a pa-

- tronage dividend that is attributable to the patron's allocable share of patronage earnings of a marketing cooperative or a supply cooperative.
 - "(2) Supply cooperative.—A 'supply cooperative' is a cooperative that sells goods or service to patrons and provided patronage dividends with respect to the quantity of purchases of the patrons.
 - "(3) Marketing cooperative.—A 'marketing cooperative' is a cooperative that sells goods produced by its members and provides patronage dividends to the members based on the quantities of goods sold or provided for sale.

"(e) Special Rules.—

- "(1) Notices of allocation and per-unit retain certificate, or other similar document shall not be treated as a patronage dividend until it is redeemed in cash or property.
- "(2) Opportunity to receive a patronage dividend in cash, but instead chooses to accept a per-unit retain certificate or a qualified notice of allocation, the patron will be treated as receiving

1	cash and simultaneously contributing to the capital
2	of the cooperative.
3	"(3) Application limited to qualified co-
4	OPERATIVES.—Under rules to be prescribed by the
5	Secretary, this section shall apply only to coopera-
6	tives to which one of the following provisions of the
7	Internal Revenue Code of 1986 would have applied
8	"(A) Section 501(c)(12) (relating to coop-
9	erative telephone companies and similar organi-
10	zations).
11	"(B) Section 501(c)(14) (relating to cer-
12	tain cooperative banks).
13	"(C) Section 521 (relating to farm co-
14	operatives).
15	"(D) Section 1381 (relating to coopera-
16	tives generally).
17	"(4) REGULATIONS.—The Secretary shall pre-
18	scribe regulations for the application of this section
19	The regulations shall generally be consistent with
20	subchapter T of chapter 1 of the Internal Revenue
21	Code of 1986 except to the extent that such rules
22	are inconsistent with provisions of this chapter.
23	"Subchapter J—Sourcing Rules

[&]quot;Sec. 265. Exports of property or services.

[&]quot;Sec. 266. Imports of property or services.

[&]quot;Sec. 267. Import or export of services.

[&]quot;Sec. 268. International transportation services.

- "Sec. 269. International communications.
- "Sec. 270. Insurance.

"SEC. 265. EXPORTS OF PROPERTY OR SERVICES.

- 2 "(a) General Rule.—Taxable receipts do not in-
- 3 clude amounts received by the exporter thereof for prop-
- 4 erty or services exported from the United States for use
- 5 or consumption outside the United States.
- 6 "(b) Export Through Nonbusiness Entity.—
- 7 For purposes of subsection (a), if property or services are
- 8 sold to a governmental entity or a tax-exempt organization
- 9 for export and are exported other than in an activity of
- 10 such entity which is subject to the business tax, then the
- 11 seller of such property or services is deemed to be the ex-
- 12 porter thereof.
- 13 "(c) Export of Services.—See section 267 for
- 14 rules for determining whether services are exported or im-
- 15 ported.
- 16 "SEC. 266. IMPORTS OF PROPERTY OR SERVICES.
- 17 "(a) In General.—The import of property or serv-
- 18 ices for consumption in the United States shall constitute
- 19 a business purchase if such property or service is to be
- 20 used in a business activity in the United States. Property
- 21 being held for sale or retail by a business entity that is
- 22 in the business of selling goods shall be considered held
- 23 for 'use in a business activity'.
- 24 "(b) Amount of Business Purchase.—

1	"(1) In general.—The cost of business pur-
2	chases with respect to the import of property or
3	services for use or consumption in the United States
4	is the customs value, price or other amount used for
5	purposes of determining the import tax under sec-
6	tion 286 or section 287.
7	"(2) Import tax.—The cost of business pur-
8	chases does not include any import tax paid. No de-
9	duction shall be allowed with respect to property or
10	service imported by a business entity unless the im-
11	port tax is paid with respect to such import.
12	"SEC. 267. IMPORT OR EXPORT OF SERVICES.
13	"(a) In General.—Except as otherwise provided in
14	this subchapter or in rules prescribed under subchapter
15	G (relating to financial intermediation business), services
16	shall not be treated as imported or exported from the loca-
17	tion in which they are performed.
18	"(b) Import of Services.—A business entity shall
19	be treated as importing a service if—
20	"(1) the entire benefit of the service will be re-
21	alized in the United States, and
22	"(2) the benefit will be realized in connection
23	with the United States business activities of the

24

business entity.

1	"(c) Export of Services.—A business will be
2	treating as exporting a service if—
3	"(1) the entire benefit of the service will be re-
4	alized outside of the United States, and
5	"(2) the benefit will be realized solely in con-
6	nection with the activities of the purchaser occurring
7	outside the United States.
8	"(d) Services Acquired From Service Provider
9	THAT PROVIDES SERVICES IN AND OUTSIDE THE
10	United States.—
11	"(1) IN GENERAL.—If a business entity ac-
12	quires services from a service provider that provides
13	services both in and outside the United States and
14	the service provider shows on the invoice where the
15	services are provided—
16	"(A) the business entity shall treat the
17	services as provided where stated on the invoice
18	and
19	"(B) the service provider shall treat as tax-
20	able receipts any services listed as provided in
21	the United States.
22	"(2) No invoice.—If a business entity acquires
23	services from a service provider that provides serv-
24	ices both in and outside the United States and the

1	service provider does not show on an invoice where
2	such services are provided—
3	"(A) the business entity shall treat the
4	services as if provided in the location to which
5	payment is sent, and
6	"(B) the service provider shall treat as tax-
7	able receipts any payments received in the
8	United States.
9	"(e) Special Rules Prevail.—See sections 268
10	and 269 for special rule relating to transportation and
11	communication services.
12	"SEC. 268. INTERNATIONAL TRANSPORTATION SERVICES.
13	"(a) Transportation of Property.—
14	"(1) Taxable receipts.—
15	"(A) Exports.—Taxable receipts do not
16	include receipts from the transportation of
17	property exported from the United States.
18	"(B) Imports.—Taxable receipts include
19	receipts from transportation of property im-
20	ported into the United States only if such costs
21	are not taken into account in determining the
22	import tax.
23	"(C) Presumptions.—The Secretary shall
24	prescribe regulations describing situations in
25	which a transporter of property must presume

1	that no import tax has been paid on the cost of
2	its services.
3	"(2) Business purchases.—
4	"(A) Exports.—Business purchases do
5	not include amounts paid or incurred for the
6	cost of transportation of property exported from
7	the United States.
8	"(B) Imports.—Amounts paid or incurred
9	for transportation of goods imported into the
10	United States, shall constitute a cost of busi-
11	ness purchase only to the extent that they are
12	taken into account in determining the customs
13	value for purposes of section 286(a) (relating
14	to the import tax).
15	"(b) Transportation of Passengers.—
16	"(1) Taxable receipts.—Taxable receipts—
17	"(A) include receipts from the transpor-
18	tation of passengers from the United States to
19	a destination outside the United States, but
20	"(B) do not include receipts from the
21	transportation of passengers from outside the
22	United States to a destination in the United
23	States.
24	"(2) Business purchases.—Business
25	purchases—

1	"(A) include amounts paid or incurred in
2	a business activity for the transportation of
3	passengers from the United States to a destina-
4	tion outside the United States, but
5	"(B) do not include amounts paid or in-
6	curred for transportation of passengers from
7	outside the United States to a destination in
8	the United States.
9	"(3) SIMPLIFYING RULES.—The Secretary may
10	provide rules that simplify this subsection, including
11	rules under which—
12	"(A) half of receipts attributable to trans-
13	portation to or from the United States are
14	treated as taxable receipts,
15	"(B) half of the cost for business trips to
16	and from the United States are treated as busi-
17	ness purchases, and
18	"(C) all transportation expenses of a busi-
19	ness entity that has no regular business outside
20	the United States are treated as business pur-
21	chases.
22	"SEC. 269. INTERNATIONAL COMMUNICATIONS.
23	"(a) In General.—For purposes of section 266,
24	communications services shall be treated as provided at

the point of origin of the communications and shall not be treated as imported or exported. 3 "(b) Communications Services.—Communications services include— 5 "(1) telephone communications services, "(2) courier services (except in the case of 6 7 transportation of property that is imported or ex-8 ported), 9 "(3) satellite transmission services, "(4) telegraph services, 10 11 "(5) facsimile transmission services, and 12 "(6) other similar services. 13 "SEC. 270. INSURANCE. 14 "(a) IN GENERAL.—Insurance services will be treat-15 ed as provided at the location of the insurance company providing the services. Except as the Secretary may pre-16 17 scribe by regulations, insurance companies will be treated 18 as providing services at the location to which insurance 19 payments are made. 20 "(b) Insured Risks in the United States.—If 21 insurance services are provided outside the United States 22 and the insured risk is located in the United States—

"(1) the insurance service shall be treated as

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imported,

23

1	"(2) the insurance premiums shall be subject to
2	the import tax, and
3	"(3) payments of insurance benefits shall not be
4	treated as imported.
5	"(c) Insured Risk Outside the United
6	STATES.—If insurance services are provided inside the
7	United States and the insured risk is located outside the
8	United States—
9	"(1) insurance services shall be treated as ex-
10	ported,
11	"(2) payments of insurance benefits shall be
12	treated as payments for services outside the United
13	States, and shall not be deducted as business pur-
14	chases.
15	"(d) Insurance Services.—Insurance services
16	means the provision of insurance and services related to
17	insurance other than insurance that is treated as a savings
18	asset.
19	"SEC. 271. BANKING SERVICES.
20	"The Secretary shall prescribe regulations on the lo-
21	cation of banking services and the extent to which such
22	services are to be treated as imported or exported.
23	"Subchapter K—Business Conducted in a
24	Possession

"Sec. 276. Treatment of possessions.

1 "SEC. 276. TREATMENT OF POSSESSIONS.

- 2 "(a) In General.—For purposes of the business tax
- 3 imposed by this chapter, the U.S. possessions shall not
- 4 be treated as part of the United States.
- 5 "(b) Effect on Payroll Tax Credit.—A busi-
- 6 ness entity may not claim a payroll tax credit with respect
- 7 to any payroll taxes paid with respect to income of resi-
- 8 dents of the U.S. possessions.
- 9 "(c) Possession.—For purposes of this subchapter,
- 10 'U.S. possession' or 'possession' means a possession of the
- 11 United States and includes the Commonwealth of Puerto
- 12 Rico and the Virgin Islands.

13 "Subchapter L—Payroll Tax Credit

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"Sec. 281. Amount of credit.
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14 "SEC. 281. AMOUNT OF CREDIT.

- 15 "(a) Amount of Credit.—The payroll tax credit for
- 16 a business entity for a taxable year is the lesser of—
- 17 "(1) the sum of—
- 18 "(A) the current-year payroll tax credit,
- 19 and
- 20 "(B) the credit carryovers to the taxable
- 21 year, or
- "(2) the business entity's business tax for the
- taxable year (determined without regard to the pay-
- roll tax credit).

[&]quot;Sec. 282. Current-year payroll tax credit.

[&]quot;Sec. 283. Credit carryover.

1	"(b) Consolidated Returns.—In the case of busi-
2	ness entities filing consolidated returns, the amount of the
3	credit shall be determined using the combined payroll tax
4	credits and credit carryovers of the business entities and
5	the combined business tax of the business entities.
6	"SEC. 282. CURRENT-YEAR PAYROLL TAX CREDIT.
7	"(a) In General.—The 'current-year payroll tax
8	credit' is an amount equal to the sum of—
9	"(1) the employer's share of the FICA tax im-
10	posed on wages of its employees during the taxable
11	year,
12	"(2) the employer's share of the tier 1 railroad
13	retirement tax for its employees during the taxable
14	year,
15	"(3) one-half of the allocable portion of the
16	SECA tax imposed on individuals (other than inde-
17	pendent contractors and other business entities) who
18	provide services to the business entity.
19	"(b) Definitions.—
20	"(1) Employer's share of the fica tax.—
21	'Employer's share of the FICA tax' means the old-
22	age, survivors, disability and hospital insurance
23	taxes imposed by section 3111.

1	"(2) Employer's share of the tier 1 rail-
2	ROAD RETIREMENT TAX.—"Employer's share of the
3	tier 1 railroad retirement tax' means—
4	"(A) the tier 1 railroad retirement tax im-
5	posed by section 3221(a), and
6	"(B) the portion of the tax imposed by sec-
7	tion 3211(a)(1) on employee representatives at-
8	tributable to the tax imposed by section 3111.
9	"(3) One-half of the allocable portion
10	OF THE SECA TAX.—
11	"(A) SECA TAX.—'SECA tax' means the
12	self-employment tax imposed by section 1401.
13	"(B) PARTNERSHIPS.—Until such time as
14	the SECA tax and the Federal Insurance Con-
15	tributions Acts are amended to treat partners
16	of partnerships as employees, if a partner des-
17	ignates a partnership as a principal source of
18	employment income for the taxable year, one-
19	half of the partnership's allocable portion of the
20	SECA tax of such partner equals the FICA tax
21	that the employer would have been required to
22	pay under section 3111 with respect to such
23	partner if the partner's self-employment income
24	as reported by the partnership were wages sub-
25	ject to the FICA tax. A partner and partner-

- ship can agree to treat no portion of a partner's SECA tax as allocable to the partnership.
- individual who is a proprietor or sole owner and provider of service to a business entity, the individual shall allocate the portion of one-half of his SECA tax not allocated pursuant to subparagraph (B) to his business entities in accordance with rules prescribed by the Secretary.
- 10 "(c) Special Rule.—Under rules prescribed by the 11 Secretary, an individual subject to the self-employment tax
- 12 shall pay half of the self-employment tax on an amount
- 13 of self employment income not less than the amount of
- 14 the individual's self-employment income taken into ac-
- 15 count by partnerships under subparagraph (B) of sub-
- 16 section (b)(3).

17 "SEC. 283. CREDIT CARRYOVER.

- 18 "(a) Carryover.—A current-year credit that is not
- 19 applied in the taxable year in which earned shall constitute
- 20 a credit carryover until applied but for no more than 15
- 21 taxable years.
- 22 "(b) Order of Use.—For purposes of determining
- 23 which credits are applied under section 281, if the total
- 24 credit allowable in a taxable year is less than the sum of
- 25 the current-year payroll credit and the carryover credits,

- 1 the current-year payroll credit shall be considered applied
- 2 first and then credit carryovers shall be considered applied
- 3 in the order earned.

4 "Subchapter M—Import Tax

- "Sec. 286. Imposition of tax on property.
- "Sec. 287. Imposition of tax on import of services.
- "Sec. 288. General rules for the import tax.

5 "Sec. 286. Imposition of tax on property.

- 6 "(a) General Rule.—There is hereby imposed a
- 7 tax equal to 11 percent of the customs value of all prop-
- 8 erty entered into the United States for consumption, use
- 9 or warehousing.
- 10 "(b) Liability for Tax.—The tax imposed on the
- 11 import of property by subsection (a) shall be paid by the
- 12 person entering the property into the United States for
- 13 consumption, use or warehousing. Such tax shall be due
- 14 and payable at the time of import.
- 15 "(c) Imports of Previously Exported Prop-
- 16 ERTY.—In the case of any article that is classified under
- 17 a heading or subheading of subchapter I or II of chapter
- 18 98 of the Tariff Schedules of the United States, the tax
- 19 under this section shall be imposed only on that portion
- 20 of the customs value of such article that is dutiable under
- 21 such heading or subheading.
- 22 "(d) Imports for Personal Consumption.—The
- 23 import tax imposed by this section shall not apply to any
- 24 article entered into the United States duty free under sub-

- 1 chapters I through VII of chapter 98 of the Tariff Sched-
- 2 ules of the United States.
- 3 "SEC. 287. IMPOSITION OF TAX ON IMPORT OF SERVICES.
- 4 "(a) General Rule.—There is hereby imposed a
- 5 tax equal to 11 percent of the cost of all services treated
- 6 as imported into the United States during the taxable year
- 7 of the service recipient.
- 8 "(b) Liability for the Tax.—The tax on the im-
- 9 port of services imposed by subsection (a) shall be paid
- 10 by the person who receives the imported services. The tax
- 11 shall be payable as if it were an addition to the business
- 12 tax imposed by section 201.
- 13 "(c) Imported Services.—For purposes of this sec-
- 14 tion, services shall be treated as imported if they are treat-
- 15 ed as imported under section 267 (general rules on import
- 16 of services) or section 270 (related to insurance).
- 17 "(d) Special Rule for Insurance.—The seller of
- 18 insurance that is treated as imported under section 270
- 19 shall be liable for the collection of the tax imposed by sub-
- 20 section (a) on the insurance and for paying such tax to
- 21 the Secretary. The first sentence of subsection (b) (relat-
- 22 ing to the person liable for the tax) shall apply to insur-
- 23 ance only to the extent that the seller of the insurance
- 24 services does not collect such tax.

1 "SEC. 288. GENERAL RULES FOR THE IMPORT TAX.

- 2 "(a) IMPORT TAX.—'Import tax' means the tax im-
- 3 posed by section 286 on the import of property and the
- 4 tax imposed by section 287 on the import of services.
- 5 "(b) No Payroll Tax Credit.—The payroll tax
- 6 credit shall not be allowed against the import tax.

7 "Subchapter N—Transition Rules

- "Sec. 290. Amortization of transition basis.
- "Sec. 291. Sales of transition basis property.
- "Sec. 292. Safe harbor leases.
- "Sec. 293. Carryovers.
- "Sec. 294. Section 481 adjustments.

8 "SEC. 290. AMORTIZATION OF TRANSITION BASIS.

- 9 "(a) Transition Basis Deduction.—The 'transi-
- 10 tion basis deduction' for a taxable year is the sum of the
- 11 amortization allowance determined under this section for
- 12 the taxable year.
- 13 "(b) Amortization Rules.—The amortization al-
- 14 lowance for each category of amortizable basis shall be de-
- 15 termined by amortizing the amortizable basis of such cat-
- 16 egory ratably over the amortization period for the category
- 17 beginning January 1, 1999.
- 18 "(c) Amortization Period.—The amortization pe-
- 19 riods shall be determined in accordance with the following
- 20 table:

In the case of:	The amortization period is:
Category I basis	15 years
Category II basis	30 years
Category III basis	40 years
Unrecovered inventory costs	5 years

1	"(d) Categories.—
2	"(1) Category I basis.—"Category I basis' is
3	the sum of the unrecovered bases as of January 1,
4	1999, of all depreciable property placed in service
5	prior to January 1, 1999, and the unamortized por-
6	tion of amortizable costs incurred before January 1,
7	1999, if—
8	"(A) cost recovery or amortization began
9	before January 1, 1999, and
10	"(B) the remaining recovery period or am-
11	ortization period as of January 1, 1999, is less
12	than 15 years.
13	"(2) Category II basis.—"Category II basis"
14	is the sum of the unrecovered bases as of January
15	1, 1999, of all depreciable property placed in service
16	prior to January 1, 1999, and the unamortized por-
17	tion of amortizable costs incurred before January 1,
18	1999, if—
19	"(A) cost recovery or amortization began
20	before January 1, 1999, and
21	"(B) the remaining recovery period or am-
22	ortization period as of January 1, 1999, is than
23	15 years or more

1	"(3) Category III basis.—'Category III basis'
2	is the sum of the adjusted basis of each asset satis-
3	fying the following requirements:
4	"(A) The asset was placed in service prior
5	to January 1, 1999,
6	"(B) The asset was used in a business ac-
7	tivity in 1999,
8	"(C) The cost of the asset was capitalized
9	and not depreciable or otherwise recoverable
10	under the Internal Revenue Code of 1986, and
11	"(D) The cost of the asset would have con-
12	stituted deductible expenses under the business
13	tax if such cost had been incurred after 1998.
14	"(4) Unrecovered inventory costs.—'Un-
15	recovered inventory costs' means the cost of goods
16	sold (as determined under the Internal Revenue
17	Code of 1986) if a business entity sold all of its in-
18	ventory (including inventory being produced) on the
19	effective date of the business tax.
20	"(e) Rules of Application.—
21	"(1) Remaining recovery period.—
22	"(A) Time of measure.—The remaining
23	recovery period shall be determined as of De-
24	cember 31, 1998, and shall include each taxable
25	year ending after such date in which a deduc-

1	tion would have been allowed under the Internal
2	Revenue Code of 1986.
3	"(B) Accounting method.—The remain-
4	ing recovery period shall be determined using
5	the cost recovery method and rules applicable
6	for determining taxable income under the Inter-
7	nal Revenue Code of 1986.
8	"(2) Depletable assets.—Under rules pre-
9	scribed by the Secretary, this section shall apply to
10	the remaining cost basis of depletable property and
11	to other property for which a cost recovery method
12	other than one based on time is used.
13	"SEC. 291. SALES OF TRANSITION BASIS PROPERTY.
14	"(a) In General.—Except as provided in subsection
15	(b), for purposes of determining the tax consequences of
16	a sale, retirement, casualty or conversion to personal use
17	of an asset whose basis or cost is taken into account under
18	section 90, the amount to be amortized shall be treated
19	as fully deducted upon the adoption of the business tax.
20	"(b) Substantial Sales.—
21	"(1) In general.—In the case of a substantial
22	sale of assets to which the amortization rules of sec-
23	tion 90 apply, the purchaser and seller may jointly

1	deductions attributable to such assets, in which
2	case—
3	"(A) the seller's taxable receipts from such
4	sale shall be reduced by the amount of
5	unamortized basis or cost assumed by the pur-
6	chaser,
7	"(B) the purchaser may treat as a cost of
8	a business purchase only the portion of the pur-
9	chase price in excess of the amount of
10	unamortized basis or cost assumed,
11	"(C) the unamortized basis or cost as-
12	sumed shall continue to be amortized in the
13	manner amortized by the seller.
14	"(2) Substantial sale.—A sale of assets by
15	a business entity to another business entity is a sub-
16	stantial sale if—
17	"(A) more than 20 percent (in fair market
18	value or in original cost) of the assets of the
19	seller are sold,
20	"(B) the total consideration for the sale
21	exceeds \$1 million or 20 percent of the taxable
22	receipts of the seller for the taxable year pre-
23	ceding the year of the sale, or

- 1 "(C) the sale satisfies other criteria estab-
- 2 lished by the Secretary to prevent distortions in
- gross profits resulting from asset sales.

4 "SEC. 292. SAFE HARBOR LEASES.

- 5 "(a) In General.—In the case of a safe harbor
- 6 lease, rental payments deemed to occur under the lease
- 7 and interest payments deemed to be made under the leases
- 8 shall constitute costs of business purchases, and rental in-
- 9 come and interest income deemed to be earned under the
- 10 lease shall constitute taxable receipts. The transition basis
- 11 deduction rules shall apply to the lessor's adjusted basis
- 12 in assets subject to a safe harbor lease.
- 13 "(b) Safe Harbor Lease.—'Safe harbor lease'
- 14 means a sale and leaseback transaction entered into pur-
- 15 suant to section 168(f)(8) of the Internal Revenue Code,
- 16 as added by the Economic Recovery Tax Act of 1981,
- 17 when such provision was in effect but only if such trans-
- 18 action would not be treated as a sale and leaseback for
- 19 tax purposes but for that provision.

20 "SEC. 293. CARRYOVERS.

- 21 "(a) No Loss Carryovers.—No deduction shall be
- 22 allowed under the business tax for net operating loss
- 23 carryovers, capital loss carryovers, or any other loss
- 24 carryovers from the income tax under the Internal Reve-
- 25 nue Code of 1986.

- 1 "(b) No Credit Carryovers.—No credits shall be
- 2 allowed under the business tax for business credit
- 3 carryovers, minimum tax credit carryovers, or any other
- 4 credit carryovers from the income tax under the Internal
- 5 Revenue Code of 1986.
- 6 "SEC. 294. SECTION 481 ADJUSTMENTS.
- 7 "(a) Positive Net Section 481 Adjustment
- 8 Amount.—If, as of January 1, 1999, a business entity
- 9 has a positive net section 481 adjustment amount, the
- 10 amount shall be applied to reduce the transition basis in
- 11 accounts (for purposes of section 290) in the following
- 12 order:
- "(1) First, to reduce the category I basis (but
- 14 not below zero),
- 15 "(2) Second, to reduce the category II basis
- 16 (but not below zero),
- 17 "(3) Third, to reduce the unrecovered inventory
- 18 costs.
- 19 "(b) Negative Net Section 481 Adjustment
- 20 Amount.—If, as of January 1, 1999, a business entity
- 21 has a negative net section 481 adjustment amount, the
- 22 amount shall be applied to increase category I basis for
- 23 purposes of section 290.

	101
1	"(c) Section 481 Adjustment.—A business enti-
2	ty's net section 481 adjustment is determined by
3	subtracting—
4	"(1) the sum of all additional deductions to
5	which a business entity would be entitled by reason

- of section 481 of the Internal Revenue Code of 1986
- 7 for periods beginning on or after the effective date
- 8 of the business tax with respect to changes in ac-
- 9 counting methods made before such effective date,
- 10 from
- 11 "(2) the sum of all additional income which a
- business entity would recognize by reason of section
- 13 481 of the Internal Revenue Code of 1986 for peri-
- ods beginning on or after the effective date of the
- business tax with respect to changes in accounting
- methods made before such effective date,
- 17 in each case assuming that the income tax under the In-
- 18 ternal Revenue Code of 1986 remained in effect.

19 "Subchapter O—Rules for Administration,

20 Consolidated Returns

21 "SEC. 301. RETURNS, DUE DATES, ETC.

- 22 "(a) In General.—Until subtitle F is amended to
- 23 reflect the adoption of this chapter, the rules of subtitle

[&]quot;Sec. 301. Returns, due dates, etc.

[&]quot;Sec. 302. Consolidated returns.

```
1 F relating to C corporations shall apply to business enti-
   ties with respect to—
 3
             "(1) returns and records;
             "(2) time and place for paying tax;
 4
             "(3) assessment of taxes;
 5
             "(4) collections and liens;
 6
             "(5) abatements, credits, and refunds;
 7
 8
             "(6) interest on underpayments and overpay-
 9
        ments;
             "(7) additions to tax and penalties;
10
             "(8) closing agreements and compromises;
11
             "(9) crimes;
12
             "(10) judicial proceedings;
13
14
             "(11) discovery of liability and enforcement;
15
        and
             "(12) estimated taxes.
16
17
        "(b) Individuals Engaging in Business Activi-
   TIES.—Under rules prescribed by the Secretary, individ-
18
   uals engaging in business activities on their own or with
19
   their spouses shall be permitted to file their business tax
21
   returns with their individual tax returns and shall be sub-
22 ject to estimated tax rules for individual income tax re-
23 turns.
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"SEC. 302. CONSOLIDATED RETURNS.

- 2 "(a) In General.—Business entities may file con-
- 3 solidated returns of business tax if they would have been
- 4 permitted to file consolidated returns under section 1501
- 5 of the Internal Revenue Code and such section were ap-
- 6 plied by treating each business entity as a corporation and
- 7 its owners or partners as shareholders.
- 8 "(b) Financial Institutions.—Financial inter-
- 9 mediation businesses may be included in consolidated re-
- 10 turns, but each financial intermediation business must
- 11 compute its gross profits separately.
- 12 "(c) Intercompany Transactions.—In computing
- 13 the gross profits of a consolidated group, intercompany
- 14 transactions can be taken into account, or at the election
- 15 of the filer, be disregarded (except in the case of trans-
- 16 actions with financial intermediation businesses).

17 "Subchapter P—Definitions and Rules of

18 Application

19 "SEC. 310. DEFINITIONS.

- 20 "(a) In General.—When used in this chapter,
- 21 where not otherwise distinctly expressed or manifestly in-
- 22 compatible with the intent thereof—

[&]quot;Sec. 310. Definitions.

[&]quot;Sec. 311. Rules of application.

1	"(1) USA INCOME TAX.—"USA Income Tax"
2	and 'Simplified USA Tax' for individuals mean the
3	tax imposed by chapter 1.
4	"(2) Internal revenue code of 1986.—"In-
5	ternal Revenue Code of 1986' means the Internal
6	Revenue Code of 1986 as in effect immediately be-
7	fore the enactment of the Simplified USA Tax.
8	"(3) United States' means
9	the States and the District of Columbia.
10	"(b) Terms Defined in Chapter 2.—If a term
11	that is used but not defined in this chapter or in section
12	7701 is defined in chapter 1, the definition in chapter 1
13	shall apply except if manifestly incompatible with the in-
14	tent of the provision in which the term is used.
15	"SEC. 311. RULES OF APPLICATION.
16	"(a) Definitions.—Any definition included in this
17	chapter shall apply for all purposes of this chapter
18	unless—
19	"(1) such definition is limited to the purposes
20	of a particular chapter, section, or subsection, or
21	"(2) the definition clearly would not be applica-
22	ble in a particular context.
23	"(b) Interpretations Consist With Internal
24	REVENUE CODE OF 1986.—Terms not defined in this
25	chapter or elsewhere in this title, but defined in the Inter-

- 1 nal Revenue Code of 1986, shall be interpreted in a man-
- 2 ner consistent with the Internal Revenue Code of 1986,
- 3 except to the extent such interpretation would be incon-
- 4 sistent with the principles and purposes of this chapter."
- 5 (b) The amendments made by this section shall be
- 6 effective on January 1, 1999, except to the extent other-
- 7 wise specifically provided in the text of such amendments.
- 8 SEC. 302. REPEAL OF CHAPTER 6.
- 9 Chapter 6 of the Code (relating to consolidated re-
- 10 turns) is repealed as of January 1, 1999.

11 TITLE IV—DEFERRED

12 **COMPENSATION PLANS**

- 13 SEC. 401. PROVISIONS SAVED.
- 14 (a) In General.—Excepts as otherwise provided in
- 15 this title, the sections contained in subchapter D of chap-
- 16 ter 1 of the Code (relating to deferred compensation, etc.)
- 17 are hereby saved as chapter 3.
- 18 (b) LIMITATIONS ON CHAPTER 3.—The following
- 19 new section is inserted before section 401 of the Code (as
- 20 saved by subsection (a)):
- 21 "SEC. 400. EFFECT OF CHAPTER 3.
- 22 "(a) In General.—The provisions of chapter 3 (sec-
- 23 tions 401 through 420) are included in this subtitle for
- 24 purposes of cross-reference and for purposes of determin-
- 25 ing whether plans are exempt from the business tax and

- 1 whether contributions to plans are deductible or exclud-
- 2 able from gross income under chapter 1.
- 3 "(b) Effect on Business Tax Deductions.—
- 4 Notwithstanding any provision to the contrary in this
- 5 chapter, no provision of this chapter shall cause any
- 6 amount to be treated as a cost of business purchase or
- 7 to otherwise be deducted from gross receipts for purposes
- 8 of computing the Simplified USA for Tax Businesses
- 9 under chapter 2.
- 10 "(c) No Credits.—Notwithstanding any provision
- 11 to the contrary in this chapter, no provision of this chapter
- 12 shall result in a tax credit against any tax imposed by
- 13 chapter 1 or chapter 2.
- 14 "(d) Effect of Failure To Comply With Provi-
- 15 Sions.—A failure to comply with applicable provisions in
- 16 this chapter could cause a plan to lose its exemption from
- 17 the business tax and, thereby subject certain business ac-
- 18 tivities of the plan to the business tax and/or result in
- 19 the constructive distribution of plan assets to plan partici-
- 20 pants."
- 21 (c) Section 408A Susperseded by Section 30.—
- 22 Section 408A is repealed.
- 23 SEC. 402. CLERICAL AMENDMENTS.
- 24 (a) Table of Sections.—The table of sections for
- 25 subpart A of part 1 of chapter 3 of the USA Tax Code

1	(formerly subchapter D of chapter 1 of the Code) is
2	amended by inserting at the beginning of the table:
3	"CHAPTER 3—DEFERRED COMPENSATION,
4	ETC."
5	(b) Renumbering of Chapters.—
6	(1) Renumber Chapters.—Chapters 2 and 3
7	of the Code are renumbered 4 and 5 respectively.
8	Such renumbering shall be reflected in all tables and
9	headings in the Code.
10	(2) Cross references.—Any cross reference
11	to chapter 2 or 3 of the Code contained in any provi-
12	sion of the Code that is not amended by this Act or
13	in any other statute shall be treated as a reference
14	to such chapter as renumbered by paragraph 1.
15	TITLE V—REPEAL OF ESTATE
16	AND GIFT TAXES
17	SEC. 501. REPEAL OF GRATUITOUS TRANSFER TAXES.
18	Subtitle B of the Code (relating to estate and gift
19	taxes) is repealed.
20	SEC 502. EFFECTIVE DATE.
21	Section 501 shall apply to—
22	(1) gifts made after December 31, 1998;
23	(2) the estates of decedents dying after Decem-
24	ber 31, 1998, and

1	(3) generating skipping transfers (within the
2	meaning of subchapter B of chapter 13 as in effect
3	before its repeal by this Act) occurring after Decem-
4	ber 31, 1998.
5	TITLE VI—TECHNICAL AND AD-
6	MINISTRATIVE CHANGES: EF-
7	FECTIVE DATES
8	SEC. 601. USA TAX CODE.
9	(a) Redesignation of the Code.—The Internal
10	Revenue Title enacted August 16, 1954, and as heretofore
11	and hereby amended may be cited as the "USA Tax
12	Code". The USA Tax Code, as hereinafter amended, may
13	be cited as the "USA Tax Code, as amended".
14	(b) References in Laws, Etc.—Except where in-
15	appropriate, any reference in any law, Executive order, or
16	other document—
17	(1) to the Internal Revenue Code of 1954 or
18	the Internal Revenue Code of 1986 shall include a
19	reference to the USA Tax Code or the USA Tax
20	Code, as amended,
21	(2) to the USA Tax Code or the USA Tax
22	Code, as amended, shall include a reference, with re-
23	spect to periods before January 1, 1999, to the In-
24	ternal Revenue Code of 1954 or the Internal Reve-
25	nue Code of 1986.

1 SEC. 602. REVISIONS TO THE CODE.

2	Not later than January 1, 2000, the Secretary shall
3	submit to Congress proposed changes in the USA Tax
4	Code that—
5	(1) eliminate cross-references to the Internal
6	Revenue Code of 1986 (except with respect to tran-
7	sition issues) and insert provisions similar to the
8	cross-referenced sections of the Internal Revenue
9	Code of 1986,
10	(2) revise subtitles C through J of the USA
11	Tax Code to fully reflect the amendments to subtitle
12	A of the Code made by this Act and the repeal of
13	subtitle B,
14	(3) include statutory definitions or rules in
15	cases where the Secretary concludes that the defini-
16	tions or rules cannot or should not be addressed by
17	regulation,
18	(4) revise chapter 4 of the USA Tax Code (as
19	renumbered by section 402 of this Act) (relating to
20	the self-employment tax) to conform to changes
21	made by this Act, and
22	(5) revise chapter 5 of the USA Tax Code (as
23	renumbered by section 402 of this Act) (relating to
24	withholding on nonresident aliens and foreign cor-
25	porations) to reflect changes made in this Act.

SEC. 603. APPLICATION OF SUBTITLE F.

- 2 Until such time as subtitle F of the Code is amended
- 3 to reflect the amendments made by this Act, the provisions
- 4 of subtitle F shall be treated as generally applying to the
- 5 Simplified USA Tax—
- 6 (1) without regard to specific cross references,
- 7 (2) without regard to provisions relating to
- 8 partnerships, and
- 9 (3) as if the business tax under chapter 2 were
- 10 the corporate income tax and all business entities
- were corporations (except for purposes of collection,
- in which case the owners of noncorporate entities
- shall be obligated for taxes owned by the entities to
- 14 the same extent as they would if the entity owed the
- tax prior to the amendment of the Code).
- 16 SEC. 604. CLERICAL AMENDMENT.
- 17 The portion of the table at the beginning of the Code
- 18 listing subtitles and chapters of subtitle A is amended to
- 19 read as follows:

"Subtitle A-Simplified USA Tax

[&]quot;Subtitle A. Simplified USA Tax.

[&]quot;Subtitle B. [deleted].

[&]quot;Subtitle C. Employment taxes.

[&]quot;Subtitle D. Miscellaneous excise taxes.

[&]quot;Subtitle E. Alcohol, tobacco and certain other excise taxes.

[&]quot;Subtitle F. Procedure and administration.

[&]quot;Subtitle G. The Joint Committee on Taxation.

[&]quot;Subtitle H. Financing of presidential election campaigns.

[&]quot;Subtitle I. Trust Fund Code.

[&]quot;Subtitle K. Group health plan requirements.

[&]quot;Chapter 1. Simplified USA Tax for individuals.

[&]quot;Chapter 2. Simplified USA Tax for businesses.

- "Chapter 3. Deferred compensation plans.
- "Chapter 4. Tax on self-employment income.
- "Chapter 5. Withholding of tax on nonresident aliens and foreign corporations."

1 SEC. 605. EFFECTIVE DATES.

- 2 (a) In General.—Except as otherwise provided in
- 3 this Act, the amendments made by this Act shall be effec-
- 4 tive on January 1, 1999, with respect to tax years begin-
- 5 ning or such date.
- 6 (b) Special Rules for Businesses With 52–53
- 7 WEEK YEAR.—If a business uses a 52–53 week taxable
- 8 year the amendments made by this Act shall apply to the
- 9 business with respect to its tax year beginning in the last
- 10 week in December except with respect to any transactions
- 11 occurring during 1998 that were structured to take advan-
- 12 tage of the application of this Act to such business at a
- 13 time when this Act did not apply to other businesses or
- 14 to individuals.

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